III. RATE STRUCTURE MODIFICATIONS

A. Common Line

2. Subscriber Line Charge

1. *Raising or eliminating the SLC cap on non-primary residential lines and multi-line business lines.* Several commenters, including incumbent LECs, IXCs, and cable companies support the proposal to raise or eliminate the SLC cap for multi-line business customers and for residential lines beyond the primary connection to the level necessary to recover the full per-line loop costs assigned to the interstate jurisdiction.[2] Several incumbent LECs are not opposed to raising the SLC for multi-line businesses, but are opposed to increasing the SLC for non-primary residential lines.[3] BA/NYNEX states that raising the SLC cap for multi-line business lines is an appropriate, but small step towards correct recovery of NTS costs.[4] Ad Hoc supports increasing the SLC cap for multi-line business and non-primary residential lines as long as users of those lines do not pay more than the costs the incumbent LEC incurs to

---

[2] *See, e.g.,* Ameritech Comments at 11-12; American Carriers Telecommunication Association (ACTA) Comments at 7; Telecommunications Resellers Association (TRA) Comments at 34-35; Association for Local Telecommunications Services (ALTS) Comments at 24-25; Teleport Communications Group Inc. (Teleport) Comments at 24-25, Reply at 14-16; Time Warner Communications Holdings, Inc. (Time Warner) Comments at 8; Tele-Communications, Inc. (TCI) Comments at 10. *See also* BellSouth Corporation and BellSouth Telecommunications, Inc. (BellSouth) Comments at 69-70 (stating that if the Commission does not provide universal support for second lines, SLC cap for unsupported lines should be removed, giving incumbent LECs the flexibility to raise the SLC on those lines).

[3] *See, e.g.,* United States Telephone Association (USTA) Comments at 56; Bell Atlantic Telephone Companies and NYNEX (BA/NYNEX) Comments at 33; U S West, Inc. (U S West) Comments at 56-57; Southern New England Telephone Company (SNET) Comments at 35; Pacific Telesis Group (PacTel) Comments at 6, 63.

[4] BA/NYNEX Comments at 33.

provide those lines.[5] SWBT, PacTel and GSA/DOD support raising the SLC to recover NTS common line costs, but argue that because loop costs are the same for residential and business lines, there is no economic justification for imposing different SLCs for these lines.[6]

2. Several LECs opposing the proposal to raise the SLC on non-primary residential lines contend that in addition to imposing new charges on the end-user, this method of cost recovery would be administratively burdensome, because no practical way exists to identify second residential lines or lines into second homes.[7] BA/NYNEX argues that charging different SLCs on second lines would require information collection and verification procedures that are not in place today.[8] Other parties also argue that eliminating or raising the SLC cap on additional residential lines will create the incentive for customers to "game" the system by reporting their additional lines under different names or by obtaining additional lines from competitors to avoid paying an additional SLC.[9] BA/NYNEX, PacTel, and Citizens Utilities argue that if the Commission adopts a cost-recovery mechanism that raises the SLC on second residential lines, it should be optional.[10]

3. Most non-price cap LECs and several state commissions and consumer groups oppose increasing or eliminating the SLC cap for multi-line business lines and for residential lines beyond the primary connection.[11] Rural carriers and Internet providers are concerned

[5] Ad Hoc Telecommunications Users Committee (Ad Hoc) Comments at 10-11; Reply at 4.

[6] Southwestern Bell Telephone Company (SWBT) Comments at 12; PacTel Comments at 61-62; General Services Administration/United States Department of Defense (GSA/DOD) Comments at 11.

[7] *See, e.g.*, USTA Comments at 56, Reply at 33; BA/NYNEX Comments at 33; BellSouth Comments at 69; PacTel Comments at 63, Reply at 21; Cincinnati Bell Telephone Company (Cincinnati Bell) Comments at 7-8; National Exchange Carrier Association, Inc. (NECA) Reply at 7-8; Rural Telephone Coalition (Rural Tel. Coalition) Reply at 12-13.

[8] BA/NYNEX Comments at 33.

[9] *See, e.g.*, PacTel Comments at 63, Reply at 21-22; Cincinnati Bell Comments at 7; John Staurulakis, Inc. (Staurulakis) Comments at 8; NECA Comments at 13; Roseville Telephone Company (Roseville Tel.) Comments at 9-10; Minnesota Independent Coalition Comments at 13; Washington Independent Telephone Association (WITA) Comments at 5; Illinois Commerce Commission (Illinois Commission) Comments at 9.

[10] BA/NYNEX Comments at 33-34 (arguing that those LECs that choose not raise SLCs on additional residential lines should retain their CCL recovery); PacTel Reply at 22; Citizens Utilities Company (Citizens Utilities) Comments at 28-29.

[11] *See, e.g.*, Staurulakis Comments at 8-9; GVNW Inc./Management (GVNW) Comments at 6-7, Reply at 6; Roseville Tel. Comments at 9-10; Harris, Skrivan & Associates, LLC (Harris, Skrivan & Associates) Comments at 6; ITCs, Inc. (ITC) Comments at 3; WITA Comments at 5; State Consumer Advocates Comments at 21-22; Rural Tel. Coalition Comments at 7-8; Reply at 12-13; Public Utilities Commission of Ohio (Ohio Commission)

about the potential negative impact that raising or eliminating the SLC cap on second and additional residential lines and multi-line business lines will have on rural areas. These commenters argue that by reducing demand for additional access lines, this proposal would have a negative impact on Internet usage and economic growth in rural areas.[12] TCA asserts that a reduction in demand for additional access lines will increase the cost of remaining lines, placing an additional burden on the Universal Service fund.[13] Parties opposed to raising the SLC cap also argue that, especially in light of the Universal Service Joint Board's recommendation not to support multi-line business lines and residential lines beyond the primary connection, raising SLCs for these lines will make them unaffordable in rural communities, violating section 254(b) which requires that all consumers have access to rates and services that are "reasonably comparable" with those provided in urban areas.[14]

4. Frontier, Sprint, and AT&T contend that raising the SLC cap only for additional residential lines and multi-line business lines will not solve the problem of uneconomic recovery of loop costs.[15] These IXCs and other commenters, including LECs, consumer groups, and wireless and cable companies, urge the Commission to raise or eliminate the SLC caps on all lines, thus permitting LECs to recover all of the interstate allocated costs of the local loop from end-users.[16] Some of these parties argue that because IXCs do not cause the costs associated with the local loop, assigning any portion of the costs associated with the

Comments at 3, Reply at 3; Public Utility Commission of Texas (Texas Commission) Comments at 6-7; Minnesota Independent Coalition Comments at 12-13; TDS Telecommunications Corporation (TDS) Comments at 3-4, 20-21, Reply at 4; Georgia Public Service Commission (Georgia Commission) Reply at 12-13; Missouri Public Service Commission (Missouri Commission) Comments at 3; Western Alliance Comments at 22-24; Commercial Internet Exchange Company (CIEA) Comments at 13, Reply at 9-11; Competition Policy Institute Comments at 18; Microsoft Corporation (Microsoft) Comments at 5.

[12] *See, e.g.*, Harris, Skrivan & Associates Comments at 6; TCA Telecommunications Corporation (TCA) Comments at 4; GVNW Comments at 7; Staurulakis Comments at 7-9; Western Alliance Comments at 22-24; ITC Comments at 3; NECA Comments at 13, Reply at 7-9; Rural Tel. Coalition Comments at 8; Pennsylvania Internet Service Providers Comments at 8-9;
CIEA Comments at 13; Reply at 10.

[13] TCA Comments at 4.

[14] *See, e.g.*, ITC Comments at 3; Rural Tel. Coalition Comments at 8, Reply at 11; TDS Comments at 3-4, Reply at 4; Western Alliance Comments at 23; TCA Comments at 3-4.

[15] Frontier Corporation (Frontier) Comments at 6-8; Sprint Corporation (Sprint) Comments at 11-12, 17; AT&T Corp. (AT&T) Reply at 27.

[16] *See, e.g.*, GTE Service Corporation (GTE) Comments at 26-29; SWBT Comments at 37-38; Cincinnati Bell Comments at 6-7; AT&T Comments 51-54, Reply at 25-26; Frontier Comments at 4, 5-7; Sprint Comments at 11-15; 50-51; Ad Hoc Reply at 4; GSA/DOD Comments at 9-11, Reply at 5, 7; TCI Comments at 10; Time Warner Comments at 4-5; WorldCom, Inc. (WorldCom) Comments at 30-31.

loop to the IXCs is economically inefficient.[17] Sprint contends that raising the SLC cap for residential users is unlikely to have a significant effect on subscribership.[18] WorldCom states that a subscriber loop is a fixed facility dedicated to the end user and that once the loop has been ordered and installed, the incumbent LEC incurs no additional costs for additional traffic passing over that loop.[19]

5. Several parties that oppose raising the SLC cap argue that the common line is a joint and common or shared cost that should be recovered from IXCs and other service providers, as well as from the end user.[20] The Texas Public Utility Counsel disagrees with Sprint's assertion that raising the SLC cap will have minimal effect on subscribership.[21] State consumer advocates and the Oregon Commission favor eliminating the SLC entirely and allowing all common line costs to be recovered from the IXCs.[22]

6. USTA and J. Staurulakis argue that because the common line revenue requirement is a much larger percentage of total costs for rate-of-return LECs than it is for most price cap LECs, any changes in the SLC cap adopted for price cap LECs should not be extended to rate-of-return LECs.[23] Roseville argues that any change to the SLC should be optional for rate-of-return LECs.[24]

7. The Illinois Commission, U S West, and Pennsylvania Internet Service Providers argue that if the Commission raises the SLC cap, the increase should be phased in over time.[25]

---

[17] *See, e.g.*, AT&T Comments at 51-54, Reply at 28; Frontier Comments at 5; Sprint Comments at 11.

[18] Sprint Comments at 12.

[19] WorldCom Comments at 28-29.

[20] *See, e.g.*, American Association for Adult and Continuing Education, *et al.* Comments at 13, Reply at 7-8; Georgia Commission Reply at 11; Rural Tel. Coalition Reply at 4-5; National Association of Regulatory Utility Commissioners (NARUC) Comments at 3, 13.

[21] Texas Office of Public Utility Counsel (Texas Public Utility Counsel) Reply at 4-10.

[22] *See, e.g.*, State Consumer Advocates Comments at 24-27; Texas Public Utility Counsel Comments at 11, Reply at 15; Public Utility Commission of Oregon (Oregon Commission) Comments at 4-5.

[23] USTA Comments at 56-57; Staurulakis Comments at 7-8.

[24] Roseville Tel. Comments at 9-10. *See also* Minnesota Independent Coalition Comments at 5 (arguing that any change to the CCL rate structure should be optional).

[25] Illinois Commission Comments at 10; U S West Comments at 53-55; Pennsylvania Internet Service Providers Comments at 11-12.

WorldCom and Ad Hoc oppose any transition period for a rate structure change.[26] Ad Hoc states that because an increase in the SLC for second and additional residential lines and multi-line business lines would not result in service disruptions, a transition period is not needed and would delay implementation of an efficient common line rate structure.[27] GVNW asserts that a three-year transition period would not be sufficient in a number of cases.[28]

8. *Geographic Deaveraging of the SLC.* The Illinois Commission and several incumbent LECs argue in favor of allowing LECs to deaverage SLCs.[29] They argue that an averaged SLC creates cross-subsidies between high-cost and low-cost areas, in violation of the 1996 Act and that deaveraging the SLC is economically efficient and consistent with cost-causation principles. Several of these parties state that the Commission should permit SLC deaveraging to the same extent that unbundled network elements or network access lines are deaveraged, *i.e.,* within the same geographic areas.[30] Sprint contends that LECs should be required to deaverage the SLC.[31] BA/NYNEX and US West argue that geographic deaveraging should be optional.[32] The Ohio Commission argues that although it may be necessary to deaverage the SLC based on differing loop costs among the individual service areas in an incumbent LEC's service territory, the deaveraged rates must not exceed the current SLC caps.[33]

9. The Washington Utilities and Transportation Commission and BA/NYNEX argue that section 254(e) does not require deaveraged SLC rates.[34] State Consumer Advocates and the New York Commission argue that geographic averaging of the SLC is not an implicit

[26] WorldCom Comments at 32; Ad Hoc Comments at 11-12.

[27] Ad Hoc Comments at 11-12.

[28] GVNW Comments at 7.

[29] Illinois Commission Comments at 10; U S West Comments at 56, Reply at 28; Ameritech Comments at 12-13, Attachment B at 19; BellSouth Comments at 32; GTE Comments at 30-31; PacTel Comments at 62-63. See *also* Sprint Comments at 17, 42.

[30] Illinois Commission Comments at 10-11; Ameritech Comments at 12; BA/NYNEX Comments at 46, n.105. *See also* ALLTEL Comments at 11 (supporting geographic deaveraging of SLC based on a minimum of three pricing zones).

[31] Sprint Comments at 17, 42.

[32] BA/NYNEX Comments at 34; U S West Comments at 56, Reply at 28.

[33] Ohio Commission Comments at 5, Reply at 5.

[34] Washington Utilities and Transportation Commission (Washington Commission) Comments at 5; BA/NYNEX Comments at 34.

subsidy that is inconsistent with the requirements of section 254(e).[35] BA/NYNEX explains that rates should not be considered subsidized simply because they are averaged, because any rate that is not developed on a customer-specific basis involves averaging.[36] BA/NYNEX also states, however, that if the SLC is deaveraged, it should be subject to the existing $6.00 and $3.50 caps.[37] The Washington Commission states that deaveraged rates may be appropriate in the future, if adequate universal service mechanisms are in place.[38]

10. Several commenters oppose deaveraging the SLC.[39] These parties argue that deaveraging the SLC violates the "comparable services and comparable rates" requirement of section 254 and will increase local rates in high-cost areas or increase the burden on the Universal Service Fund. The Texas Public Utility Counsel argues that deaveraging rates is inconsistent with market practices and the social policy embodied in the 1996 Act.[40] It argues further that deaveraging SLC costs would complicate the calculations of Universal Service subsidies and make it more difficult for long distance companies to maintain geographically averaged rates, as required by section 254(g).[41] Time Warner agues that the Commission should not permit geographic deaveraging of SLCs at this time because it will give incumbent LECs opportunity to engage in anticompetitive conduct.[42]

3. Carrier Common Line Charge

11. Most commenters agree that the per-minute CCL charge is economically inefficient because it does not reflect the way in which underlying loop costs are incurred and sends incorrect signals into the marketplace, encouraging inefficient use of

[35] State Consumer Advocates Comments at 48-49; New York State Department of Public Service (New York Commission) Comments at 7-8.

[36] BA/NYNEX Comments at 34.

[37] *Id.* at 46, n. 105.

[38] Washington Commission Comments at 5.

[39] See, e.g., Minnesota Independent Coalition Comments at 14; TDS Comments at 3, 20; Rural Tel. Coalition Reply at 10; State of Hawaii (Hawaii Commission) Reply at 3, 12-14; Pennsylvania Internet Service Providers Comments at 12-13.

[40] Texas Public Utility Counsel Comments at 13.

[41] *Id.* at 14.

[42] Time Warner Comments at 8-9.

telecommunications services and uneconomic bypass of incumbent LEC facilities.[43] BellSouth states that recovering more common line costs through NTS per-line charges "would greatly enhance economic welfare primarily because it would reduce the marginal cost of interstate long-distance calls and therefore would greatly expand interstate long-distance calling."[44] Some commenters state that the CCL charge functions as an implicit cross-subsidy from long distance access to local service, and from high-volume users to low-volume users.[45] Although most parties agree that the CCL charge structure should be revised so that incumbent LECs are no longer required to recover any of the NTS costs of the loop from IXCs on a traffic-sensitive basis, they disagree on the best approach to use for assessing that charge.

12. *Flat Per-Line Charge.* Many commenters, including both price cap and non-price cap incumbent LECs, IXCs, and some state commissions support recovering all common line costs or the common line costs not recovered through the SLCs through a flat, per-line charge assessed against the customer's PIC.[46] Several of these parties also support the proposal to bill the customer directly in cases where the customer has not chosen a PIC.[47] Supporters of

---

[43] *See, e.g.*, Ameritech Comments at 9; BA/NYNEX Comments at 32; PacTel Comments at 58-64, Reply at 21; SWBT Comments at 35-36; Rural Tel. Coalition Comments at 6; ACC Long Distance Corp. (ACC Long Distance) Comments at 10-11; AT&T Comments at 51-54, Reply at 25-26; MCI Telecommunications Corporation (MCI) Comments at 77; LCI International Telecom Corp. (LCI) Comments at 20-21; WorldCom Comments at 28-29; Frontier Comments at 4; NECA Comments at 10; Ad Hoc Comments at 8-11; Time Warner Comments at 2-4; Winstar Communications (WinStar) Comments 3-5; Teleport Comments at 22-24; GSA/DOD Comments at 7-8; Competition Policy Institute Comments at 1-7; California Cable Television Association Comments at 10; NARUC Comments at 11-12; Public Service Commission of the District of Columbia (District of Columbia Commission) Comments at 3-4; U.S. Department of Justice (DOJ) Comments at 11, 14-15. *But see,* Evans Telephone Company, *et al.* (Evans, *et al.*) Comments at 4-5 (stating that current mix of recovery mechanisms is an appropriate compromise).

[44] *See* Letter from Robert T. Blau, BellSouth, to Mr. William F. Caton, Acting Secretary, FCC (filed April 25, 1997) at Attachment 1: "Economically-Efficient Access Reform" by Robert W. Crandall, The Brookings Institution, at 1.

[45] WorldCom Comments at 30; Ameritech Comments at 9; GTE Comments at 18, 26.

[46] *See, e.g.*, USTA Comments at 55-56; BA/NYNEX Comments at 35-36; BellSouth Comments at 68, Reply at 10-11; PacTel Comments at 64, Reply at 21; U S West Comments at 54-55; Citizens Utilities Comments at 27-28; Roseville Tel. Comments at 4, 8; Rural Tel. Coalition Comments at 6, Reply at 9; CompTel Comments at 29; Cable & Wireless, Inc. (Cable & Wireless) Comments at 10; Excel Telecommunications, Inc. (Excel) Comments at 11; LCI Comments at 20-21, Reply at 6; MCI Comments at 77; District of Columbia Commission Comments at 3-4; South Dakota Public Utilities Commission (South Dakota Commission) Comments at 3; NARUC Comments at 13; National Cable Television Association, Inc. (NCTA) Comments at 26; American Communications Services, Inc. Reply at 17.

[47] *See, e.g.*, USTA Comments at 55-56, Reply at 32; BA/NYNEX Comments at 36; U S West Comments at 54-55; Citizens Utilities Comments at 27-28; Roseville Tel. Comments at 8; WorldCom Comments at 37; District of Columbia Commission Comments at 3-4; Ad Hoc Reply at 4-5.

this approach state that converting the common line charge to a per-line flat charge paid by the customer's IXC is administratively simple and will allow IXCs to recover their costs through a variety of pricing plans, as the market will allow.[48] USTA and BA/NYNEX state that recovering the common line costs through a flat, per-line charge paid by the IXCs will improve economic efficiency and will rebalance rates so that high-volume customers do not overpay, and low-usage customers do not underpay, for interstate use of the local loop.[49] BA/NYNEX, SWBT, and U S West support the flat, per-line charge but argue that if the Commission adopts such a rate structure, it would need to adjust the price cap formula because the existing formula assumes the ability of the LECs to apply usage-based rates to recover network costs that are largely non-traffic sensitive.[50] The Rural Telephone Coalition and Minnesota Independent Coalition assert that a flat-rated, non-traffic sensitive common line charge would be feasible for rate-of-return LECs.[51]

13. Several parties support the proposal to recover common line costs through a flat, per-line charge assessed against the PIC but are opposed to permitting LECs to bill end-users who have not selected a PIC.[52] Cincinnati Bell argues that billing end users who have not selected a PIC would create administrative difficulties because it would require the LEC to prorate charges for both the end user and the IXC when the customer leaves an IXC in the middle of a billing cycle.[53] NARUC suggests that if a customer uses another carrier for other services, a per line charge could be divided among all carriers using the common line on the basis of relative use by the carrier.[54] NARUC opposes any solution that would effectively impose additional flat charges on the end-user.[55]

14. Others commenters state that they support the proposal to assess IXCs a flat, per-line charge as a second-best approach in the event the Commission declines to increase or eliminate the SLC cap, or if increasing the SLC is insufficient to allow incumbent LECs to

[48] *See, e.g.* BA/NYNEX Comments at 35-36; BellSouth Comments at 68 and Attachment 2 at 21-22, Reply at 11; Roseville Tel. Comments at 8; State Consumer Advocates Reply at 6; NARUC Comments at 13.

[49] USTA Comments, Attachment 1 at 7; BA/NYNEX Comments at 35.

[50] BA/NYNEX Comments at 36; SWBT Comments at 58-59; U S West Comments at 55.

[51] Rural Tel. Coalition Comments at 7; Minnesota Independent Coalition Comments at 6.

[52] *See, e.g.*, Cincinnati Bell Comments at 9-10; Puerto Rico Telephone Company (Puerto Rico Tel.) Comments at 10-13; Rural Tel. Coalition Comments at 6-7.

[53] Cincinnati Bell Comments at 9.

[54] NARUC Comments at 13.

[55] *Id.* at 12.

recover all of their interstate loop costs.[56] PacTel advocates recovering residual loop costs not recovered from an increase in the SLC through bulk billing IXCs on the basis of presubscribed lines.[57] TCI supports the proposal to assess IXCs a flat, per-line rate as a temporary measure, stating that to ensure economic efficiency, common line costs should be directly assigned to the SLC.[58]

15. The Competition Policy Institute and AARP *et al.* argue that the common line costs should be recovered from all telecommunications providers including wireless, enhanced service, and "dial around" providers based on the amount of carriage.[59] Similarly, Alliance for Public Technology proposes that the carrier common line charge and subscriber line charge be replaced with a "common facilities" charge imposed on all telecommunication carriers who use the local network to deliver services.[60] PacTel opposes the proposals made by Competition Policy Institute and Alliance because they would require a usage-sensitive charge.[61]

16. Parties opposed to the flat, per-line charge assessed on IXCs argue that recovering common line costs on a flat-rate basis from IXCs will allow IXCs to pass the cost on to customers as higher rates, reducing demand for long distance service. They further argue that this type of cost recovery will distort the market by encouraging IXCs to bypass the switched network using competitive access providers and by creating a disincentive for IXCs to compete for low-volume long distance users.[62] Other parties argue that the proposal imposes an additional administrative burden on LECs and does not adequately address the problem of

---

[56] *See, e.g.,* Ad Hoc at 11-13, Reply 4-5; Cincinnati Bell Comments at 9, Reply at 5-7; Sprint Comments at 14; WorldCom Comments at 30-33; Time Warner Reply at 28.

[57] PacTel Comments at 6, 64. *See also* SWBT Reply at 8-9 (arguing that CCL remaining after adjustments for universal service, LTS, payphone, marketing expense and reallocations to reduce the TIC should be recovered on a flat-rated basis billed to IXCs on a presubscribed line basis as a "public policy element").

[58] TCI Comments at 10-11; Reply 4-5

[59] Competition Policy Institute Comments at 14-17; American Association for Retired Persons, *et al.* (AARP, *et al.*) Comments at 13-14.

[60] Alliance for Public Technology Comments at 5.

[61] PacTel Reply at 22. *See also* Personal Communications Industry Association (PCIA) Reply at 4 (stating that Alliance's facility charge proposal is inconsistent with the cost-causative principles set forth in the NPRM).

[62] *See, e.g.,* GTE Comments at 29; GSA/DOD Comments at 9-10, Reply at 6.

"dialing around" the switched network.[63] AT&T and Sprint claim that assessing a flat, presubscribed line charge on IXCs would not eliminate the inefficiencies or the implicit cross-subsidies embedded in the CCL charge.[64] These carriers assert that a flat-rated per-line recovery mechanism would force IXCs to subsidize other service providers, including LECs, wireless carriers, ISPs, and resellers that originate or terminate traffic over the loop but are not subject to the charge. They contend that this would be inconsistent with section 254(b) which requires "equitable and nondiscriminatory contribution to universal service" by all telecommunications providers.[65] Sprint asserts that a flat-rated charge assessed on IXCs will force IXCs to adopt two-part tariffs to avoid being undercut by the usage-based rates of carriers that rely on 10XXX dial-around traffic for their business, but that would not be assessed common line charges.[66]

17. *Alternative Recovery Methods.* Several state commissions and incumbent non-price cap LECs support the proposal to recover the CCL charge through bulk billing.[67] The Oregon Commission, ACTA, and the Florida Commission favor recovering the interstate portion of loop costs through a capacity charge assessed on carriers based upon the number of switch trunk ports purchased from the incumbent LEC.[68] The Missouri Commission, the Texas Commission, and the Alabama Commission favor the proposal to assess common line charges based on the number of trunk port and line port connections an IXC has to the switched network.[69] NECA requests flexibility for pool members to recover the CCL charge through either a per-line charge and/or a bulk billing method.[70] Specifically, NECA proposes a method allowing the pool members to charge a nationwide average CCL per-line rate and

---

[63] ALLTEL Comments at 11; Illinois Commission Comments at 6-7; Ameritech Comments at 10-11; ACTA Comments at 6.

[64] AT&T Reply at 28; Sprint Comments at 15-16.

[65] AT&T Reply at 28-29; Sprint Comments at 15-16.

[66] Sprint Comments at 16.

[67] *See, e.g.,* Ohio Commission Comments at 4; Florida Public Service Commission (Florida Commission) Comments at 2; Illinois Commission Comments at 7; Alaska Telephone Association Comments at 10; ALLTEL Comments at 12; Frederick & Warinner, L.L.C. (Frederick & Warinner) Comments at 4; GVNW Comments at 6; Harris, Skrivan & Associates Comments at 6; Roseville Tel. Comments at 8; Puerto Rico Tel. Comments at 11-12; WITA Comments at 4-5.

[68] Oregon Commission Comments at 4-5; ACTA Comments at 5; Florida Commission Comments at 2.

[69] Missouri Commission Comments at 3; Texas Commission Comments at 4-5; Alabama Public Service Commission (Alabama Commission) Comments at 6.

[70] NECA Comments at 10.

bulk bill any residual amount.[71]

18. Cable & Wireless, MCI, Teleport, and others oppose the bulk billing, capacity charge, and trunk port charge alternatives because they are based on minutes of use and do not accurately reflect costs.[72] ACTA asserts that bulk billing causes operational and administrative problems.[73] According to Teleport and GCI, bulk billing ensures total recovery for the LEC because the LEC receives the same revenues whether it faces no competition or substantial competition.[74] Several commenters oppose these alternative recovery mechanisms because they are based on historical usage or revenue data.[75] Sprint argues that if a cost recovery mechanism is based on historical usage or revenue data, an interexchange carrier that is losing market share will be penalized, while a carrier whose market share is growing will receive a windfall.[76]

19. The Minnesota Independent Coalition and TCA argue that a capacity charge based on trunks is not feasible for smaller LECs because most IXCs serving smaller LECs do not use dedicated trunks.[77] MCI and the Minnesota Independent Coalition argue that imposing NTS costs based on the relative number of trunks or ports may encourage IXCs to use fewer trunks or ports than are needed, leading to adverse impacts on service quality.[78]

20. Ameritech proposes to recover common line costs via a Loop/Port recovery charge that it would assess as a single, aggregate charge per carrier on IXCs based upon their percentage share of state- or region-wide interstate retail revenues.[79] Sprint and Time Warner

[71] *Id. See also* NECA Reply at 6-7.

[72] *See, e.g.,* Cable & Wireless Comments at 10; MCI Comments at 77; Sprint Comments at 13-14; Teleport Comments at 28; People of the State of California and the Public Utility Commission of the State of California (California Commission) Comments at 4.

[73] ACTA Comments at 6.

[74] Teleport Comments at 28; General Communication, Inc. (GCI) Reply at 10.

[75] Sprint Comments at 13; ALTS Comments at 24-25, Reply at 23; American Communications Services, Inc. Reply at 17.

[76] Sprint Comments at 13.

[77] Minnesota Independent Coalition Comments at 6-7; TCA Comments at 3.

[78] Minnesota Independent Coalition Comments at 7; MCI Comments at 77.

[79] Ameritech Comments at 9-10. Ameritech states that it would initially set its LPR at the revenues from the CCL charge, less payphone and long-term support, plus line-side port costs from local switching plus the information charge, and would transition the LPR to cost over 5 years. *Id.*

oppose Ameritech's proposal, stating that such an approach would insulate incumbent LECs from the forces of competition.[80] According to Sprint, long distance carriers entering the local market through unbundled network elements or their own facilities or that purchased access from new entrants would be required to pay Ameritech regardless of the extent to which they utilized Ameritech's loops or switching.[81] Time Warner states that Ameritech's proposal ensures the survival of the local loop bottleneck by eliminating opportunities for low-cost new entrants to compete in the provisioning of local loops.[82]

21. *Impact of 254(g) on Carrier Common Line Charge Recovery*. Excel and the Alaska Commission argue that section 254(g) does not impose any limitations on the Commission's authority to assess flat-rated CCL charges on IXCs because the section pertains to rates charged to "subscribers" or the ultimate end-user, not other carriers.[83] The majority of commenters responding to this inquiry argue that section 254(g) prohibits IXCs from passing their flat-rated charges through to end users on a deaveraged basis.[84] USTA argues that although the flat-rate CCL charged to the IXCs should be deaveraged by customer and by region to be consistent with cost-causation principles, it will not conflict with section 254(g) because IXCs can average any disparate flat-rate CCL charges into their rate structure as they have averaged disparate per-minute CCL charges.[85] Sprint and WorldCom argue that forbearance from Section 254(g) would be warranted.[86] Sprint asserts that if incumbent LECs continue to recover NTS costs, particularly common line costs, from the IXCs and these costs are recovered through deaveraged rates charged to the IXCs, forbearance from section 254(g) would be warranted because of the magnitude and variability of these costs.[87] WorldCom argues that IXCs should be free to recover subscriber loop costs assessed by incumbent LECs through a flat charge per line or through any other rate recovery mechanism the long distance

[80] Sprint Reply at 12-13; Time Warner Reply at 16-17.

[81] Sprint Reply at 12-13.

[82] Time Warner Reply at 16-17.

[83] Excel Comments at 11; State of Alaska (Alaska Commission) Reply at 3-4;

[84] *See, e.g.,* State Consumer Advocates Comments at 49-51; Rural Tel. Coalition Comments at 27-30; Minnesota Independent Coalition Comments at 8-9,11; Harris, Skrivan & Associates Comments at 7; TDS Comments at 3, 19-20, Reply at 21; Alaska Commission Reply at 3-4; Hawaii Commission Reply at 2.

[85] USTA Comments, Attachment 1 at 7-8, Reply at 33. *See also* Tennessee Regulatory Authority (Tennessee Commission) Comments at 3.

[86] Sprint Reply at 27; WorldCom Comments at 34.

[87] Sprint Reply at 27.

market will allow.[88] WorldCom argues further that unless the Commission forbears with respect to application of section 254(g), IXCs will be forced to average common line costs and recover them through long distance rates--a cross-subsidy that runs counter to the overall policies of section 254(b) and (c).[89] Several parties oppose forbearance.[90]

4. Common Line PCI Formula

22. Incumbent LECs argue that TFP incorporates growth into the X-Factor, and that retaining the current separate common line formula would tend to double-count growth.[91] Some of those incumbent LECs assert that a separate common line formula might impede certain access reforms that they support.[92] Lincoln claims that common line demand growth output would be reflected as common line output growth in a TFP calculation, and so would transfer the benefits of demand growth to IXCs.[93] Sprint and AT&T maintain that the Commission must retain a separate common line formula, regardless of how the X-Factor is calculated.[94] AT&T argues that a separate common line formula is necessary to avoid giving more revenues to the LECs with the highest common line costs, and to recognize the IXCs' role in promoting common line demand growth.[95] AT&T also asserts that the LECs' claims

---

[88] WorldCom Comments at 34-35.

[89] *Id.*

[90] Harris, Skrivan and Associates Comments at 7; Minnesota Independent Coalition Comments at 11; Rural Tel. Coalition Comments at 28-30.

[91] USTA Comments in Price Cap Fourth Further NPRM at 44-45; GTE Comments in Price Cap Fourth Further NPRM at 41-42; Southwestern Bell Comments in *Price Cap Fourth Further NPRM* at 35-36; BellSouth Comments in Price Cap Fourth Further NPRM at 42; Bell Atlantic Comments in Price Cap Fourth Further NPRM at 14; Frontier Comments in Price Cap Fourth Further NPRM at 10; Ameritech Comments in Price Cap Fourth Further NPRM at 8-9; Lincoln Telephone (Lincoln) Comments in *Price Cap Fourth Further NPRM* at 15; U S West Comments in Price Cap Fourth Further NPRM at 25-26; NYNEX Comments in Price Cap Fourth Further NPRM at 29; PacTel Comments in Price Cap Fourth Further NPRM at 15; USTA Reply in Price Cap Fourth Further NPRM at 27-28; U S West Reply in Price Cap Fourth Further NPRM at 34; Frontier Reply in Price Cap Fourth Further NPRM at 5-6; Ameritech Reply in Price Cap Fourth Further NPRM at 3.

[92] NYNEX Comments in Price Cap Fourth Further NPRM at 31; Ameritech Reply in Price Cap Fourth Further NPRM at 3; USTA Reply in Price Cap Fourth Further NPRM at 28.

[93] Lincoln Reply in Price Cap Fourth Further NPRM at 9-10 and Attachment A.

[94] Sprint Comments in Price Cap Fourth Further NPRM at 12; AT&T Comments in Price Cap Fourth Further NPRM at 43.

[95] AT&T Reply in Price Cap Fourth Further NPRM at 57-60.

of double-counting growth have not been adequately substantiated.[96]

23. Southwestern Bell argues that the g/2 term should be removed from the common line formula because common line minutes of use grow more quickly than number of access lines. Southwestern Bell asserts that flat CCL charges would reduce incumbent LECs' revenue growth by about 0.5 percent per year.[97]

5. Assessment of SLCs on Derived Channels

24. *Pleadings filed in response to the ISDN SLC NPRM.*[98] Only one commenter, AT&T, favors retaining the current approach for PRI ISDN service. AT&T does not support assessing a SLC per derived channel for BRI service, but instead favors assessing a SLC for each BRI facility. All of the other parties, including the other IXCs, oppose it. ISDN users, LECs, and equipment manufacturers argue that retaining the current rule will deter ISDN deployment, and will discourage development of new technologies.[99] Almost all of the LECs, user groups, equipment manufacturers, IXCs, and other commenters support a rule that would assess a SLC for each pair of copper wires,[100] or a SLC for each ISDN facility.[101]

---

[96] *Id.* at 59.

[97] SWBT Comments at 58-59. According to Southwestern Bell, for the incumbent price cap LECs, CCL minutes of use grew at an average annual rate of 6.8 percent from 1991 to 1995, while access lines grew at an average of 3.0 percent. *Id.* at 59. *See also* BA/NYNEX Comments at 36; U S West Comments at 55; USTA Reply, Attachment 3 at 9-10.

[98] Comments filed in response to our ISDN SLC NPRM, End User Common Line Charges, CC Docket No. 95-72, Notice of Proposed Rulemaking, 10 FCC Rcd 8565 (1995), will be referred to as ISDN Comments and ISDN Reply.

[99] America Online Incorporated, CompuServe Incorporated, GE Information Services, Inc., and Prodigy Services Company (America Online) ISDN Comments at 8-10 (citing *U.S. Industrial Outlook* 1994, U.S. Department of Commerce at 25-1, January 1994, and citing Bell Atlantic Waiver Petition at 7-8, which estimates that requiring a SLC per derived channel would reduce demand for BRI service by about 60 percent and demand for PRI service by about 35 percent). *See also* Cable & Wireless ISDN Comments at 3-4; Microsoft Corporation (Microsoft) ISDN Comments at 4; West Virginia University ISDN Comments at 1; TCA ISDN Comments at 4; Information Technology Industry Council (ITIC) ISDN Reply at 3; Roseville Tel. ISDN Reply at 4; Northern Telecom Inc. (Nortel) ISDN Reply at 5; The Bell Atlantic Telephone Companies (Bell Atlantic) ISDN Reply at 3.

[100] *See, e.g.*, Roseville Tel. ISDN Comments at 2; TCA ISDN Comments at 1; Tennessee Commission ISDN Comments at 2-3.

[101] *See e.g.*, Ameritech ISDN Comments at 2; BellSouth ISDN Comments at 4-5; Cincinnati Bell ISDN Comments at 3, 6; NTCA ISDN Comments at 1-2; NYNEX ISDN Comments at 16; SWBT ISDN Comments at 3; USTA ISDN Comments at 2; 3Com Corp. ISDN Reply at 6.

Some commenters express a preference for one of these approaches, but urge the Commission to adopt one or the other of the two options.[102] Some parties further assert that, if the Commission fails to adopt a rule that assesses a SLC per copper pair or per service, it should adopt a rule based on the actual non-traffic-sensitive costs of providing derived channel services compared to costs of providing conventional local loops.[103] Numerous trade groups, ISDN users, and LECs assert that a SLC per pair of copper wires or a SLC per facility approach would encourage use of advanced services, such as ISDN, that offer numerous potential benefits.[104]

25. The parties also assert that assessing a SLC per facility or pair of copper wires would best reflect the underlying purpose of the SLC, which is to recover non-traffic-sensitive loop costs.[105] Some parties also assert that charging a SLC per facility is consistent with the Commission's goals of eliminating unreasonable discrimination and undue preferences among rates for interstate services, using the local network efficiently, preventing uneconomic bypass, and preserving universal service.[106] Others argue that this approach is administratively simple,[107] that it will reduce the opportunity for uneconomical pricing by competitors,[108] and

[102] GTE ISDN Comments at 9-10; ITIC ISDN Comments at 2; NTCA ISDN Comments at 2; Northern Arkansas Telephone Company ISDN Comments at 2-4; CIEA ISDN Reply at 1; 3Com Corporation ISDN Reply at 6-7.

[103] Rural Tel. Coalition ISDN Comments at 4-5; American Petroleum Institute (API) ISDN Comments at 6. *See also* Northern Arkansas Telephone Company ISDN Comments at 2-3 (suggesting that assessing 7 or 8 SLCs for PRI service might be reasonable, based on costs).

[104] America Online ISDN Comments at ii, 1-3; ITIC ISDN Comments at 3-4; Center for Democracy and Technology ISDN Comments at 3; National Public Radio ISDN Comments at 3-4; Microsoft ISDN Comments at 2; Pacific Bell ISDN Comments at 1-2; TCA ISDN Comments at 3. Some parties assert that ISDN will set the new telecommunications standard, competing with, or even replacing, plain old telephone service (POTS). Pacific Bell ISDN Comments at 3; ITIC ISDN Comments at 3. *See also* Northern Arkansas Telephone Company ISDN Comments at 3-4; Center for Democracy and Technology ISDN Comments at 3. Others describe ISDN as a significant but interim step in the development of an advanced communications network. Microsoft ISDN Comments at 2; TCA ISDN Comments at 3-4.

[105] Roseville Tel. ISDN Comments at 2; USTA ISDN Comments at 9; NYNEX ISDN Comments at 3; BellSouth ISDN Comments at 4-5; Pacific Bell ISDN Comments at 4-5; Roseville Tel. ISDN Reply at 3 (asserting that any charge beyond one SLC per service over-recovers non-traffic-sensitive costs).

[106] USTA ISDN Comments at 8; Roseville Tel. ISDN Comments at 2; Cable & Wireless ISDN Reply at 2.

[107] GTE ISDN Comments at 9-10; SWBT ISDN Comments at 3-4; TCA ISDN Comments at 2; ITIC ISDN Comments at 1-2.

[108] USTA ISDN Comments at 15-16.

that it will reduce the likelihood of migration from switched access to dedicated service.[109]

26. Many parties, including LECs and ISDN users, argue that any method for assessing SLCs should be based on the costs of providing ISDN service.[110] Parties opposing the proposal to assess SLCs for derived channel services based on the cost ratio allege that such an approach is too complicated,[111] and that the potential benefits of this approach are outweighed by the substantial effort required to make such a cost comparison.[112] Others object that the proposal set forth in the ISDN SLC NPRM would not take into account the relevant costs. Some companies assert that ISDN service does not increase the average loop costs.[113] Others contend that the additional costs incurred to provide ISDN service are switching costs rather than common line costs.[114]

27. Few parties commented on our proposal to impose a SLC for every two derived channels. Those who did generally opposed it for many of the same reasons they opposed assessing a SLC per derived channel. For example, parties asserted that such a rule would bear no relationship to the cost of providing service, and would discourage subscription to derived channel services.[115]

---

[109] API ISDN Comments at 4; Microsoft ISDN Comments at 3; USTA ISDN Comments at 14.

[110] U S West ISDN Comments at 4; California Bankers' Clearing House ISDN Comments at 3-4;Texas Commission ISDN Comments at 6. Some parties that support a cost-based approach contend that assessing one or two SLCs are adequate to recover non-traffic-sensitive line costs of derived channel services. *See* Pacific Bell ISDN Comments at 4; Rochester Telephone Corp. ISDN Comments at 3; TCA ISDN Comments at 2; Tennessee Commission ISDN Comments at 3-4.

[111] USTA ISDN Comments at 12 (urging that it would be difficult to break down average subscriber loop costs without doing the same for other categories of subscribers); AT&T ISDN Comments at 6-7; GTE ISDN Comments at 17.

[112] America Online ISDN Comments at 6-7 (the Commission has discretion to balance strict cost-causation with the need to avoid imposing costs on new technologies that could undermine the economic viability of those technologies); Time Warner ISDN Comments at 5.

[113] SWBT ISDN Comments at 9. *But see* Bell Atlantic Comments at 4-5 and n.13 (recognizing that PRI ISDN service may increase common line costs). *See also* Tennessee Public Service Commission ISDN Comments at 3 (digital upgrades should be considered to be normal part of network evolution, and extra SLCs should not be assessed as a result of such normal network upgrades).

[114] TCA ISDN Comments at 5 and Time Warner ISDN Comments at 5. *See also* NYNEX ISDN Comments at 8-9; Sprint ISDN Reply at 1-2 (U S West proposal improperly includes non-loop plant costs such as line cards, and SLCs are based on average costs rather than service-specific costs. U S West's proposal would necessitate a fundamental reworking of the Commission's Part 69 rules).

[115] SWBT ISDN Comments at 9.

28. Several parties also filed comments regarding other modifications to access charges and our price cap rules.[116] In addition, NYNEX asserts that the Commission should not apply the rule we adopt to derived channel technologies that are not apparent to the end user and that are exclusively in the LEC's network infrastructure.[117] NYNEX claims that it would be impossible to identify the subscribers served by such technology, and that it would be inappropriate to treat those subscribers differently.

29. The BOCs subsequently provided data on the relative non-traffic-sensitive costs of single and derived channel services, in response to our request for information.[118]
As shown in Table 1 below, the cost data submitted in response to the *ISDN SLC NPRM* indicates that the ratio of NTS loop costs of BRI ISDN to standard analog service is approximately 1 to 1. The ratio of NTS loop costs of PRI ISDN to standard analog service, excluding NYNEX's data, is roughly 5 to 1. As shown in Table 2, NYNEX's data appear to be outliers and are therefore excluded from the calculation of the average ratio for PRI ISDN to standard analog service because the ratios of its outside plant and NTS costs for PRI ISDN to standard analog service are almost twice those of other incumbent LECs.

---

[116] *See, e.g.,* SWBT ISDN Comments at 3, 10; Roseville Tel. ISDN Comments at 4; MCI ISDN Comments at 5; NYNEX ISDN Comments at 5; USTA ISDN Comments at 12-13; Time Warner ISDN Comments at 4; America Online ISDN Reply at 8; Pacific Bell ISDN Comments at 5, 7.

[117] NYNEX ISDN Comments at 14.

[118] In their responses, three of the BOCs, BellSouth, NYNEX, and SWBT, asked for confidential treatment of portions of the information submitted. NYNEX publicly filed the information we requested, but submitted as confidential additional information that contained more detailed cost data. The confidential data were not necessary to perform our analysis, and the following tables only include data that was filed on the public record. We have returned to the respective companies data for which confidential treatment was sought.

TABLE 1

Ratio of costs of standard analog service to BRI ISDN service

	Outside Plant (loop only) costs	All NTS costs
Ameritech	1:1.07	1:1.45
Bell Atlantic	1:1.01	1:1.36
NYNEX	1:0.85	1:1.23
Pacific Bell	1:1.05	1:1.13
US West	1:0.80	1:1.07
Average ratio of costs	**1:0.96***	**1:1.24***

TABLE 2

Ratio of costs of standard analog service to PRI ISDN service

	Outside Plant (loop only) costs	Outside Plant (loop only) costs (excluding NYNEX	All NTS costs	All NTS costs (excluding NYNEX data)
Ameritech	1:5.68	1:5.68	1:8.9	1:8.9
Bell Atlantic	1:4.13	1:4.13	1:15.80	1:15.80
NYNEX	1:10.94	excluded	1:27.74	excluded
Pacific Bell	1:4.67	1:4.67	1:8.70	1:8.70
US West	1:5.33	1:5.33	1:10.60	1:10.60
Average ratio of costs	**1:6.5***	**1:4.95***	**1:15.13***	**1:10.5***

*Averages may differ due to rounding.

30. GTE and MCI filed comments, and America Online, NYNEX, Pacific Bell, Southwestern Bell, and US West filed reply comments in response to the cost data. Several of those parties contend that cost ratios should not be used to determine the number of SLCs to be assessed for derived channel services, because SLCs currently are set at arbitrary levels, and do not reflect the actual costs of providing any particular service.[119] Several parties also contend that, even if we decide to assess SLCs for derived channel services based on the relative non-traffic-sensitive costs of those services, we should not include switching costs such as trunk or line cards in our assessment of costs.[120] They argue that a cost-based ratio would be complex to develop, and would create substantial and unnecessary recordkeeping burdens.[121] Many parties also assert that the cost data demonstrate that there is no difference between the non-traffic-sensitive loop costs for standard analog service and BRI service, and that there is not a significant difference in the non-traffic-sensitive loop costs between standard analog service and PRI service,[122] or between digital PBX trunks and PRI service.[123]

31. *Comments filed in response to the Access Reform NPRM.* Comments filed in the current proceeding are consistent with those filed in response to the ISDN SLC NPRM. The majority of commenters support a rate structure that assesses one SLC per ISDN facility,[124] or

[119] GTE ISDN Comments regarding cost data at 3; America Online ISDN Reply regarding cost data at 2; NYNEX ISDN Reply regarding cost data at 3-4.

[120] GTE ISDN Comments regarding cost data at 4; America Online ISDN Reply regarding cost data at 2; ISDN NYNEX Reply regarding cost data at 3-4.

[121] GTE ISDN Comments regarding cost data at 4-7; NYNEX ISDN Reply regarding cost data at 4; SWBT ISDN Reply regarding cost data at 3.

[122] GTE ISDN Comments regarding cost data at 8-10; America Online ISDN Reply regarding cost data at 2 (any difference between providing PRI service and single channel service "is not large and principally is attributable to the fact that PRI ISDN is provided using two twisted copper pairs" rather than one); SWBT ISDN Reply regarding cost data at 3-4 (urging the Commission to assess one SLC per service as an interim rule, pending a separate proceeding on access charge reform). *Accord* Pacific Bell ISDN Reply regarding cost data at 3-4. *See also* U S West ISDN Reply regarding cost data at 1-2 (urging the Commission to bifurcate the treatment of BRI and PRI service, and to issue a decision immediately that would require LECs to assess no more than one SLC for BRI service).

[123] MCI ISDN Comments regarding cost data at 2; NYNEX ISDN Reply regarding cost data at 4.

[124] *See, e.g.*, USTA Comments at 56, Reply at 34; Ameritech Comments at 13; PacTel Comments at 65; GTE Comments at 33; Cincinnati Bell Comments at 8; Sprint Comments at 18; API Comments at 30-32; Compuserve Comments at 19-21, Reply at 9; Microsoft Comments at 7; PSINet Reply at 11; CIEA Comments at 12, Reply at 12; Alarm Industry Communications Committee Reply at 13.

per pair of copper wires.[125]
State Consumer Advocates, argues that assessing SLC based on pairs of wires would inhibit the introduction of new technologies and service because LECs would have a financial incentive to keep customers on conventional service.[126] TDS recommends assessing one SLC charge on a BRI ISDN line and no more than two SLCs on a PRI ISDN line.[127] Ad Hoc argues that although assessing SLCs based on derived channels should recover the costs of providing such channels, the Commission has not provided sufficient information to determine whether a ratio of 1.24 to 1 for BRI, and 10.5 to 1 for PRI accurately reflect the costs of those services.[128] PacTel argues that ISDN service is not an interstate service and, therefore, not within the Commission's jurisdiction.[129]

32. Those commenters that oppose assessing a SLC per derived channel argue that imposing one SLC per channel discourages demand for advanced services and inhibits technological development.[130] USTA states that the current multiple SLC rule imposes disproportionate burdens of cost recovery on ISDN users and that changing to a single SLC per facility would be consistent with the objectives of this proceeding.[131]

B. Local Switching

1. Non-Traffic Sensitive Charges

33. The majority of commenters agree with our tentative conclusion that cost-causative principles indicate that costs associated with line cards, line-side ports, and those trunk ports associated with dedicated transport should be recovered through flat-rated

[125] ACTA Comments at 7; Frontier Comments at 7, n.12; Alarm Industry Communications Committee Reply at 13.

[126] State Consumer Advocates Comments at 64-66.

[127] TDS Comments at 22.

[128] Ad Hoc Comments at 13-14.

[129] PacTecl Comments at 65.

[130] *See, e.g.*, SWBT Comments at 13; TCA Comments at 4; ACTA Comments at 7; CompTel Comments at 29-30; Interactive Services Association Comments at 3.

[131] USTA Comments at 56, Reply at 34.

charges.[132] Several incumbent LECs argue that there is no need to codify specific rate elements for local switching costs and, instead, advocate flexibility in the rate structure for local switching.[133] BA/NYNEX amplifies this argument by stating that it may be both difficult to quantify the NTS portion of local switching costs, and burdensome to separately charge for trunk ports based on the type of transport used by an IXC.[134] BellSouth claims that an adequately-sized universal service fund could replace all implicit support currently provided through interstate access charges that recover NTS costs, thereby reducing the carrier common line charge to zero and recovering fully the NTS portion of local switching charges.[135] The Georgia Commission argues that the assertion that NTS local switching costs are related to the provision of universal service is tantamount to saying that most costs are related to universal service and that the USF should not be the first place to look for recovery of any cost element.[136]

34. Several small LECs and the State Consumer Advocates argue that changes to the rate structure to recover NTS local switching costs on a NTS basis should be left to the Joint Board on Separations.[137] These commenters state that local switching costs formerly were recovered through a combination of TS and NTS charges and that new Parts 32 and 36, when adopted, consolidated these mechanisms because of difficulties in separating the TS and NTS costs of digital switches.[138] Therefore, these commenters argue that, if part of the costs of local switching are to recovered through NTS flat-rated charges, the Joint Board should first expand Part 36 and 69 categories related to NTS local switching equipment.[139] Otherwise, the inconsistent treatment of some local switching costs as TS for purposes of Part 36 but NTS for purposes of Part 69 would improperly transfer costs from the interstate to the intrastate

[132] *See, e.g.*, CompTel Comments at 31; USTA Comments, Attachment 1 at 8; AT&T Comments at 55; LCI Comments at 21; PacTel Comments at 66; Rural Tel. Coalition Comments at 9; Alabama Commission Comments at 7-8; Florida Commission Comments at 2; Texas Commission Comments at 8; TCI Reply at 7.

[133] *See, e.g.*, USTA Reply at 34-35; SNET Comments at 37; BA/NYNEX Comments at 39.

[134] BA/NYNEX Reply at 35.

[135] BellSouth Reply at 10; *see also* USTA Reply at 34.

[136] Georgia Commission Reply at 21.

[137] Frederick & Warinner Comments at 5; Harris, Skrivan & Associates Comments at 6; State Consumer Advocates Comments at 31-32.

[138] *E.g.*, Frederick & Warinner Comments at 5-6; Harris, Skrivan & Associates Comments at 6.

[139] Frederick & Warinner Comments at 5; State Consumer Advocates Comments at 31-32.

jurisdictions.[140]

35. U S West, Sprint and other commenters argue that to the extent that NTS line-side costs are attributable to the end user, they ought to be recovered from end users.[141] Others, such as TCI, favor an increased SLC, but support a PIC-based charge as a second-best option for recovering NTS local switching costs.[142] Ameritech and ALLTEL propose that NTS local switching costs be recovered by a charge assessed on IXCs on the basis of interstate retail service revenues or minutes of use.[143] Sprint responds that such proposals do not recover these costs on a cost-causative basis, and insulate the incumbent LEC from competition.[144] TCI maintains that the cost of the trunk side ports dedicated to an individual IXC varies directly with the number of trunks dedicated to that IXC.[145] TCI also states, however, that the costs of trunk ports associated with dedicated transport need to be recovered through a separate rate element because an IXC may use a trunk port supplied by the incumbent LEC without using the incumbent LEC's dedicated transport.[146]

36. MCI notes that identifying TS and NTS costs of local switching is not simple, and supports adoption of the proposed rate structure only if cost studies allocating costs between TS and NTS can be performed.[147] The record reflects widely varying estimates of the portion of local switching costs that are NTS. USTA estimates that the NTS portion of local switching costs ranges from 6% for analog switches to 51% for modern, digital switches.[148] ALLTEL reports that NTS local switching costs make up 31 percent of its interstate local

---

[140] State Consumer Advocates Comments at 31-32.

[141] *See, e.g.*, U S West Reply at 29; Sprint Comments at 18; Illinois Commission Comments at 11; SWBT Comments at 8; AT&T Reply at 29 (line cards that terminate a subscriber's loop should be flat-rated and charged to the subscriber via the SLC).

[142] TCI Reply at 7; *see also* BellSouth Reply at 11-12 (the mere possibility, speculative at best, that per line charges assessed on IXCs will encourage "dial-around" services, is insufficient reason for the Commission not to establish per line NTS recovery of NTS costs); Sprint Reply at 12-13.

[143] Ameritech Comments at 14; ALLTEL Comments at 12.

[144] Sprint Reply at 12-13.

[145] TCI Comments at 12.

[146] *Id.*

[147] MCI Comments at 81-82; *see also* BA/NYNEX Reply at 35 (it may be difficult to quantify the NTS portion of these costs).

[148] USTA Comments, Attachment 2 at 31.

switching revenue requirement.[149] SWBT claims NTS local switch costs could be recovered through a flat charge of $0.35 a month per line.[150] Sprint, in contrast, estimates that one-third of local switching costs are NTS, and that recovering those costs directly from end users would add $0.80 per month to end user bills.[151] Cable & Wireless reports that, based on data submitted by NYNEX, at least 49 percent of the local switching costs are NTS for modern switches.[152]

37. Cable & Wireless and other commenters state that many components of the local switch, such as the central processing portion of the switch, switch fabric, and the trunk-side ports that are not associated with dedicated transport, are shared. These commenters assert that these shared facilities should be priced on a usage-sensitive basis.[153] BellSouth, however, states that in addition to the costs of line cards and the main distribution frame, many other switching costs, *e.g.*, the cost of the switching matrix, depend substantially on the number of lines rather than usage.[154] The Texas Commission disagrees, noting that while growth in the number of dedicated lines or trunks attached to the switch does cause the central processing unit to grow in size, it is usage of these lines or trunks that cause costs.[155] The Rural Tel. Coalition states that, because small carriers lack economies of scale and scope, rural switching costs are higher per minute or per line than urban switching costs.[156]

---

[149] ALLTEL Comments at 12.

[150] SWBT Comments at 8.

[151] Sprint Comments at 18. In developing this estimate, Sprint used a TELRIC cost study of its New Jersey operations and assumed that the resulting data were representative of price cap LECs as a whole. Sprint estimates that, if end users were charged directly $0.80 monthly for local switching, this change would save IXCs $1.365 billion annually.

[152] Cable & Wireless Comments at 12-13.

[153] Cable & Wireless Comments at 12-13; Citizens Utilities Comments at 30; GSA/DOD Comments at 4.

[154] BellSouth Comments, Attachment 2 at 14 (Haring and Rohlfs, "Economic Perspectives on Access Charge Reform").

[155] Texas Commission Comments at 11-12; *see also* USTA Comments, Attachment 2 at 31 (notes that the determination of which switch to install is clearly a traffic-sensitive decision).

[156] Rural Tel. Coalition Comments at 10.

2. Traffic Sensitive Charges

38. Many IXCs, consumer groups, ESPs, and LECs oppose the establishment of a mandatory call setup charge.[157] Collectively, they raise two primary concerns: (1) the costs of call setup are *de minimis* or difficult to separate from other TS costs;[158] (2) the costs of measuring, tracking and billing for call setup would outweigh the costs of the call setup itself.[159]

39. AT&T argues that a such a mandatory charge would be inconsistent with the rate structure the Commission mandated for the local switching unbundled network element (UNE) because no call setup charge has been established as part of the unbundled local switching rate structure at either the state or federal level.[160] In addition, AT&T argues that a separate rate element is unnecessary because many of the costs of call setup are now allocated to signalling, and the signalling rate structure proposed in the NPRM includes signalling message charges for all calls.[161]

40. Cable & Wireless asserts that per-call setup costs are too small relative to the other TS costs of local switching to justify a new and separate rate element; therefore, any economic inefficiency resulting from collection on a per-minute basis is *de minimis* and would be offset by increased complexity in the rate structure.[162] LCI states that the current per-minute recovery mechanism has not been controversial in the past, and that imposing a call setup charge on call attempts would result in charges being assessed on a caller who has not received any service.[163] LCI states that, in addition to the LEC's setup costs, the IXC also incurs transport costs associated with call attempts that are not recovered explicitly from the

[157] *E.g.*, Cable & Wireless Comments at 13-15; Sprint Comments at 19; Bankers Clearing House Comments at 3-4; CompuServe/Prodigy Comments at 25-29, Reply at 11-12; USTA Comments, Attachment 1 at 8, Comments at 57, Reply at 35.

[158] *E.g.*, Cable & Wireless Comments at 13-15; Teleport Comments at 22.

[159] *E.g.*, Cable & Wireless Comments 14; Sprint Comments at 19; Teleport Comments at 22; Bankers Clearing House Comments at 3-4.

[160] AT&T Comments at 56, Reply at 30.

[161] AT&T Reply at 29. Although Ameritech favors the creation of a call setup charge, it asserts that over 95% of its calls are set up using SS7 technology.

[162] Cable & Wireless Comments at 13. *See also* Bankers Clearing House Reply at 3 (Call setup costs associated with call attempts are trivial, because out-of-band signalling permits the likelihood of call completion to be evaluated before a transmission path is established).

[163] LCI Comments at 25-26.

calling party.[164]

41. MCI opposes a separate call setup charge, asserting that it is unclear at best which part of the TS portion of local switching costs are sensitive to call attempts and which part is sensitive to minutes of use. In addition to signalling, MCI hypothesizes that some part of the cost of the central processor may be sensitive to call attempts. Any attempt to separate TS costs into per-message and per-minute categories could involve arbitrary assumptions and, therefore, MCI argues that TS costs of local switching should be left as per-minute charges.[165] MCI states, however, that any call setup charge the Commission does adopt should be assessed only on completed calls because, otherwise, the incumbent LEC will be able to charge for calls blocked by its own switch and will have reduced incentives to ensure quality service on its network.[166]

42. Several large corporate consumers of telecommunications services oppose the imposition of a call setup charge because they assert that the charge would cause churn and would be disruptive to consumers, especially banks with automatic teller machines and businesses that accept credit cards.[167] In addition, Bankers Clearing House argues that neither IXCs nor other third parties have the capability to track or audit call attempts, so assessment of setup charges based on call attempts raises the potential for unauditable billing errors.[168]

43. Several state commissions, incumbent LECs, and others favor the creation of a separate call setup charge. The costs of call setup, these parties argue, do not vary with the length of a call, so a per call charge, rather than the current per-minute recovery of these costs, would be more consistent with cost-causation principles.[169] In addition, under the current, per-minute recovery mechanism, long hold-time calls subsidize short calls and uncompleted calls.[170] Two years ago, the California Commission established mandatory call

[164] *Id.*

[165] MCI Comments at 82.

[166] MCI Comments at 83; *see also* Bankers Clearing House Reply at 4.

[167] CompuServe/Prodigy Comments at 25-29, Reply at 11-12; Bankers Clearing House Comments at 7-8; Ad Hoc Comments at 19-20, Reply at 3-4.

[168] Bankers Clearing House Comments at 3-4.

[169] *E.g.*, Excel Comments at 12; TRA Comments at 37; Ameritech Comments at 15; PacTel Comments at 69; Citizens Utilities Comments at 30; Frederick & Warinner Comments at 6-7; Minnesota Independent Coalition Comments at 15; Alabama Commission Comments at 8; California Commission at 2-3; Texas Commission at 14; TCI Comments at 12.

[170] PacTel Comments at 68, Reply at 23.

setup charges intrastate switched access, imposing charges on originating attempts that are handed off to the IXC's POP, and on terminating completions.[171] The California Commission states that this structure is appropriate because, at the point the call is handed off to the IXC's POP, the LEC switch has performed its function and the LEC has incurred the setup cost.[172] In addition, the California Commission reports that, under this structure, it has not encountered problems with LEC duplicity in generating deliberate incompletions.[173]

44. Several parties advocate recovery of call setup costs through a separate signalling rate element. Frederick & Warinner argues that, by performing call setup prior to dedicating a trunk to the call, LECs require fewer transport trunks; this efficiency should be passed along to IXCs in the form of lower access charges. Frederick & Warinner, therefore, suggests that we refer this issue to the Joint Board on Separations so that call setup expenses currently assigned to Central Office Equipment (COE) Category 3 and Interexchange Circuit Equipment Category 4.23 can be reassigned to a separate COE category designed to identify and recover all SS7 call setup charges.[174]

45. A number of the parties that favor the principle of a separate call setup charge assert that the Commission should permit, but not require, such a charge.[175] They argue that flexibility will allow incumbent LECs to establish rate structures that are responsive to market conditions.[176] Competition Policy Institute argues that separate call setup charges may be appropriate in light of the increasingly "bursty" use of the network.[177] The Georgia Commission argues that the multiplicity of opinions on this issue points to a need for flexibility,[178] while the Illinois Commission suggests that flexibility will allow incumbent LECs to evaluate whether, and to what extent, such revision to the rate structure would be

[171] California Commission Comments at 6, Reply at 2-3; PacTel Comments at 68.

[172] California Commission Reply at 2.

[173] California Commission Reply at 2-3.

[174] Frederick & Warinner Comments at 6 (these equipment categories are defined at 47 C.F.R. §§ 36.125, 36.126(b)(2)(iii)). *See also* TCI Comments 12-13, Reply at 9.

[175] *E.g.*, USTA Comments, Attachment 1 at 8, Comments at 57, Reply at 35; BA/NYNEX Comments at 39; BellSouth Comments at 71; PacTel Reply at 23 (PacTel does "not insist" that a call setup charge be mandatory); U S West Comments at 58; Competition Policy Institute Comments at 19; Georgia Commission Reply at 21-22; Illinois Commission Comments at 11-12.

[176] *E.g.*, BA/NYNEX Comments at 39; USTA Comments at 57.

[177] Competition Policy Institute Comments at 19.

[178] Georgia Commission at 21-22.

more efficient than the structure currently in place.[179] U S West supports the establishment of a call setup charge as a permissive rate structure, but cautions that the charge would require billing system changes, would affect different IXCs differently, and may be too small to merit a separate rate element.[180]

46. There is general agreement that LECs incur call setup costs for both completed calls and call attempts. Among commenters favoring a permissive or mandatory call setup charge, however, opinion is split as to whether the charge should be imposed on call attempts. Those parties favoring charges only for completed calls generally argue that this structure would (1) avoid the administrative burden and customer confusion associated with developing a tracking, metering and billing system for call attempts;[181] and (2) deny incumbent LECs the incentive to increase revenues by blocking calls at their own switch.[182] Those parties favoring charges for all call attempts generally argue that this structure would most closely reflect cost-causation principles.[183]

a. Peak and Off-Peak Pricing

47. Many commenters, including most IXCs, oppose the creation of either a permissive or a mandatory peak-rate structure, because the complexity of creating and implementing such a structure outweighs any benefits to be gained.[184] These commenters generally argue that: (1) it is impossible to determine peak and off-peak hours with any degree of certainty because peak hours vary with region of the country, type of service, type of user, rate zone, technological advances, and other factors;[185] (2) peak pricing structures would not send efficient market signals, would disadvantage competitors, and would have a *de minimis* impact on usage patterns and incumbent LEC network design because less than 15% of RBOC traffic is interstate access;[186] (3) no state commissions have established a peak

[179] Illinois Commission at 11-12.

[180] U S West Reply at 29.

[181] *E.g.*, Alabama Commission Comments at 8; Texas Commission Comments at 14.

[182] *E.g.*, MCI Comments at 83.

[183] *E.g.*, Ameritech Comments at 15; CompuServe/Prodigy Comments at 29; Citizens Utilities Comments at 30.

[184] *See, e.g.*, AT&T Comments at 56-57.

[185] *See, e.g.*, CompTel Comments at 31; Cable & Wireless Comments at 14; LCI Comments at 27; MCI Comments at 83; ALTS Comments at 24; ACC Long Distance Comments at 14; Sprint Comments at 19-20.

[186] AT&T Reply at 30; CompTel Comments at 31; ACC Long Distance Comments at 14.

pricing rate structure;[187] (4) peak hours may continue to shift over time as competitors enter the market and as the use of telecommuting, the Internet, and other data services increase;[188] and (5) necessary changes to carrier metering and billing systems may outweigh any benefits to be gained.[189]

48. Other commenters, including most incumbent LECs, support a rate structure under which LECs would be permitted, but not required, to price local switching on a peak rate basis. These commenters acknowledge the difficulties cited above, among others, but generally agree that, in principle, economic welfare benefits could be obtained from a peak rate structure by diverting traffic, and associated TS costs, from peak to non-peak hours.[190] Accordingly, these commenters advocate a permissive approach under which incumbent LECs would have the ability to develop peak and off-peak pricing structures on an optional basis in response to local conditions and subject to the limitations of their billing systems.[191] At least one commenter argues that such an approach would be consistent with our recent interconnection decisions.[192]

49. Only Excel supports establishment of a mandatory peak rate structure, arguing that such a structure would more accurately apportion costs among users and would more accurately reflect the incremental costs of additional network capacity during peak hours.[193]

[187] CompTel Comments at 31.

[188] Cable & Wireless Comments at 14; LCI Comments at 27.

[189] Bankers Clearing House Reply at 5-6; Citizens Utilities Comments at 30. *But see* Excel Comments at 12 (necessary changes to CABS are justified by the public policy benefits of a rate structure change).

[190] *E.g.*, GTE Reply, Appendix D at 15; USTA Comments, Attachment 1 at 8; TCI Comments at 13.

[191] USTA Comments at 57-58, Reply at 35; Ameritech Comments at 16-17; BA/NYNEX Comments at 40; BellSouth Comments at 71; U S West Comments at 58-59, Reply at 29-30; Citizens Utilities Comments at 30; Frederick & Warinner Comments at 7; Minnesota Independent Coalition Comments at 16; TDS Comments at 24; Competition Policy Institute Comments at 20; Georgia Commission Reply at 21-22; Illinois Commission Comments at 11-12; TCI Comments at 13, Reply at 10; Time Warner Comments at 11-12.

[192] Frederick & Warinner Comments at 7 (*citing Local Competition Order*, ¶¶ 756-757).

[193] Excel Comments at 12.

C. Transport

1. Entrance Facilities and Direct-Trunked Transport

50. The majority of commenters supported our tentative conclusion that flat-rate charges are appropriate for entrance facilities and direct-trunked transport service.[194] Those commenters addressing this subject agree that the costs of dedicated direct-trunked transport and entrance facilities are incurred on a flat-rate basis. Both PacTel and the California Commission note that, in California's Open Access Network Architecture and Development Proceeding, the parties reached consensus that costs of entrance facilities and direct-trunked transport should be recovered through flat-rate charges.[195] Several commenters assert that the costs of direct-trunked transport and entrance facilities vary with distance traversed and that rates for these facilities should be distance sensitive.[196] TCI supports distance sensitive flat-rate charges for direct-trunked transport, although it argues in favor of flat rate charges for entrance facilities, apparently without a distance-sensitive component.[197]

51. Some parties advocate certain adjustments in the rate structure for direct-trunked transport and entrance facilities. U S West and Sprint both suggest that, as carriers expand their use of fiber-optic ring architecture, the current distance-sensitive charges for direct-trunked transport should be replaced with "per-ring" rates because ring architecture makes transport costs less distance sensitive in densely populated areas.[198] U S West argues, therefore, that incumbent LECs should have the flexibility to restructure their rates to reflect

---

[194] *See. e.g.*, AT&T Comments at 59; Excel Comments at 13; MCI Comments at 84; Ameritech Comments at 18; BA/NYNEX Comments at 41; BellSouth Comments at 71; PacTel Comments at 69; U S West Reply at 30; Citizens Utilities Comments at 30; NECA Comments at 3-4; Alabama Commission Comments at 9; California Commission Comments at 6; Illinois Commission Comments at 12; Sprint Comments at 21; TCI Comments at 14, Reply at 11.

[195] PacTel Comments at 69; California Commission Comments at 6. *See Rulemaking on the Commission's Own Motion to Govern Open Access to Bottleneck Services and Establish a Framework of Network Architecture Development of Dominant Carrier Networks; and Investigation on the Commission's Own Motion into Open Access and Network Architecture Development of Dominant Carrier Networks*, CPUC Docket No. R.93-04-003/I.93-04-002, Consensus Costing Principles/Basic Network Functions; OANAD Cost Methodology Workshops, Filed Aug. 23, 1995 by California Telecommunications Coalition. Texas, also, has adopted flat-rates for these facilities. Texas Commission Comments at 15.

[196] *See, e.g.*, AT&T Comments at 60; MCI Comments at 84; Ameritech Reply at 29; U S West Reply at 30; Texas Commission Comments at 15.

[197] TCI Comments at 14, Reply at 11.

[198] Sprint Comments at 21; U S West Reply at 30.

this change.[199] Ameritech agrees that the current rates for entrance facilities and direct-trunked transport are properly structured, but argues that carriers should have the flexibility to offer switched access customers new technologies, such as SONET, without obtaining a Part 69 waiver or passing a public interest test.[200] SWBT asserts that tariff and rate structure distinctions between special access, direct-trunked transport, and entrance facilities should be eliminated because these distinctions cannot survive in a competitive environment and cause complex billing arrangements for shared use facilities.[201] USTA proposes more sweeping change, arguing that the Commission forbear from regulating collocated direct-trunked transport because this service meets the requirements of Section 10 of the Communications Act.[202]

52. There is considerable division among commenters as to whether incumbent LECs should be permitted to offer transport services differentiated by whether the LEC or the IXC is responsible for channel facility assignments (CFAs). MCI opposes such a differentiation for two reasons. Initially, MCI notes that, while the incumbent LECs claim they can achieve network savings by retaining control of CFAs, IXC provision of CFAs should save the LEC the costs of performing this function. Therefore, it is unclear whether costs should be greater or lower when the IXC performs the CFA. Secondly, MCI argues that, once the LEC enters the interexchange market, it could impute to itself a lower transport charge by providing the CFA to its interexchange subsidiary.[203] SWBT offers two additional reasons why CFA control should not be the basis for rate differentiation: (1) CFA control responsibilities may vary among LECs; and (2) rate differentiation based on CFA control may become untenable with respect to newer technologies, such as SONET architecture and ATM, which rely less heavily on particular dedicated channels. Currently, SWBT states that CFA control may indicate whether a facility is dedicated or shared.[204] ACTA also opposes pricing differentiation, arguing that the purchase of an incumbent LEC circuit is a simple business transaction and the purchasing IXC should be able to select where the purchased circuit resides.[205]

---

[199] U S West Reply at 30.

[200] Ameritech Comments at 17-18.

[201] SWBT Comments at 14-15. *See also* Ameritech Comments at 18 (arguing that pricing flexibility applicable to special access should be extended to functionally equivalent switched transport services).

[202] USTA Comments at 35-48.

[203] MCI Comments at 84-85.

[204] SWBT Comments at 62.

[205] ACTA Comments at 10.

53. TCI and the Washington Commission support giving the incumbent LECs the flexibility to differentiate direct-trunked transport rates based on whether the customer or the LEC performs CFA functions, as long as the LEC supports the differential with forward-looking cost data and, in the case of the Washington Commission, as long as it does not needlessly complicate the access tariff.[206]

2. Tandem-Switched Transport

a. Rate Structure

54. Except for AT&T, IXC commenters addressing the issue generally support the unitary rate structure and argue that the Commission should retain this pricing option.[207] These commenters argue that the unitary rate structure should remain available because: (1) access transport, as a service, has traditionally been offered on an end-to-end basis;[208] (2) the unitary rate structure promotes full and fair interexchange competition by allowing IXCs time to prepare their networks for fully cost-based pricing;[209] (3) the partitioned rate structure, if required, (a) could provide incentives for incumbent LECs to engage in inefficient network reconfiguration, because access customers have no control over incumbent LEC decisions on the location of tandems, but would be required to pay for access based on these decisions;[210] and (b) would necessitate new rules regulating incumbent LEC tandem deployment decisions;[211] (4) AT&T, by virtue of divestiture, inherited POPs in close proximity to a significant number of tandem switches and would therefore enjoy a significant legacy advantage over competitors;[212] (5) "common" and "dedicated" circuits often travel on the same facilities and along the same transmission routes, making disparate rate structures inappropriate;[213] (6) elimination of the unitary structure would raise the price of tandem-switched transport in relation to direct-trunked transport and would therefore discriminate

[206] TCI Comments at 14, Reply at 11-12; Washington Commission Comments at 6..

[207] *E.g.*, Cable & Wireless Comments at 15-17; CompTel Comments at 24-26, Reply at 11-13; MCI Comments at 85-86; TRA Comments at 37.

[208] Cable & Wireless Comments at 16.

[209] Cable & Wireless Comments at 15-16.

[210] Cable & Wireless Comments at 16; *see also* Texas Commission Comments at 17.

[211] Cable & Wireless Comments at 16-17.

[212] Cable & Wireless Comments at 17.

[213] CompTel Comments at 25, Reply at 11.

against smaller IXCs;[214] and (7) the unitary rate structure is the only structure consistent with the TSLRIC methodology of estimating costs.[215]

55. TRA additionally argues that the current rate structure, which allows IXCs to choose between the three-part and the unitary rate structure, is most consistent with the principles that costs should be recovered in the way that they are incurred, and from the cost causer.[216] Telco Communications Group requests that we explicitly allocate some common transport costs to dedicated transport rates because common transport facilities are sized to handle peak overflow loads from large carriers that use direct-trunked transport for most traffic.[217]

56. Sprint states that the Commission should retain the unitary rate structure because the three-part rate structure would give incumbent LECs the incentive to route traffic inefficiently by placing tandems far from IXC POPs.[218] Sprint argues that the term "direct trunking" is a misnomer because modern "hub and spoke" or "ring" network architecture often causes direct trunked circuits to travel along the same transmission routes and facilities as tandem switched transport circuits.[219] It would therefore be unfair to require users of tandem-switched transport to pay for the route through the tandem, while allowing direct-trunked transport users to pay based on airline miles between the EO and SWC.[220] According to Sprint, the three-part rate structure would skew interexchange competition in favor of AT&T, which has sufficient traffic to justify direct trunking to individual EOs, and in favor of the BOCs, which could take advantage of their own direct trunking to many of their end offices.[221] Sprint suggests that the Commission address the problem of underutilized circuits on the tandem-to-SWC route by allowing incumbent LECs to size trunk bundles between the two points to achieve a reasonable utilization factor.[222]

---

[214] CompTel Comments at 26, Reply at 13.

[215] CompTel Reply at 12-13; TRA Comments at 37.

[216] TRA Comments at 37.

[217] Telco Communications Group Comments at 6-7.

[218] Sprint Comments at 22-23, Reply at 15-16.

[219] Sprint Comments at 23, Reply at 14-15.

[220] *Id.*

[221] Sprint Comments at 22-23, Reply at 16.

[222] Sprint Reply at 15.

57. WorldCom states that the Commission should not revisit any of the transport rate structure issues, other than those remanded by the Court.[223] WorldCom offers the following principles, however, if we do decide to reexamine these issues: First, the rate structure should treat dedicated and common transport consistently because both services use the same network facilities. Traffic on dedicated circuits and common circuits travels physically on the same large multiplexed transmission pipe. Routing, most frequently, is identical. Therefore, WorldCom states that it would be unreasonably discriminatory for the Commission to make detailed changes to the rate structure or pricing of tandem-switched transport without making parallel changes to the pricing of dedicated transport.[224] Second, rate structure decisions should be based on the current forward-looking view of the interoffice network. Large capacity fiber optic facilities, including SONET rings, have made transmission costs less distance sensitive. Therefore, WorldCom states that the triangular, "pyramid" diagram the Commission included in the notice is outdated. Because routing is within the sole control of the incumbent LEC and may vary based on momentary traffic loads, the transport customer should pay for transport based on airline miles between the two end points. Pricing of a service on an other than end-to-end basis could penalize users of that service for decisions outside of their control.[225] Third, the Commission should use forward-looking cost methodologies in setting rates. Tandem switching rates based on fully allocated, embedded costs are in conflict with the *Local Competition Order* and with the price cap structure. Therefore, the Commission should reinitialize rates based either on a forward-looking cost study or on the proxy prices adopted in the *Local Competition Order*.[226] In light of these three principles, WorldCom states that it favors retaining the unitary rate structure, and disagrees with arguments that tandem-switched transport is currently underpriced.[227]

58. Most incumbent LECs, AT&T, and some state commissions advocate elimination of the unitary rate structure for tandem-switched transport.[228] These commenters generally argue that: (1) flat rates for the dedicated SWC-to-tandem link accurately reflect the manner

[223] WorldCom Reply at 26.

[224] WorldCom Reply at 27-28.

[225] WorldCom Reply at 29-32.

[226] WorldCom Reply at 33-34.

[227] WorldCom Reply at 26.

[228] AT&T Comments at 59-60, Reply at 32-33; USTA Comments at 60; Ameritech Comments at 19-20, Reply at 29; BA/NYNEX Comments at 41, Reply at 36-38; BellSouth Comments at 73; PacTel Comments at 70; SWBT Comments at 13-14; U S West Comments at 59-60; Citizens Utilities Comments at 31; GTE Reply at 24; SNET Reply at 29-31; NECA Comments at 3, Reply at 2-3, Puerto Rico Tel. Comments at 15-16; Florida Commission Comments at 3.

in which the LEC incurs costs for this facility;[229] (2) per-minute rates for the shared tandem-to-EO link correspond to the manner in which the LEC incurs the costs of that facility;[230] (3) mileage charges based on the length of each specific link ordered by a transport customer will encourage carriers to order facilities that minimize routing distances;[231] (5) the three-part rate structure will increase IXC incentives to order efficiently sized transport facilities, thereby increasing network efficiency, conserving trunk and switch capacity, and reducing the current level of underutilized facilities;[232] (6) the unitary rate structure is not competitively neutral, but was designed to avoid significant changes in the costs of transport for small LECs vis-a-vis large ones;[233] (7) the unitary rate structure prices tandem-switched transport below cost, thereby (a) creating a subsidy paid by large IXCs that use direct-trunked transport to small IXCs that use tandem-switched transport;[234] and (b) disadvantaging competitive access providers (CAPs) because they cannot compete with the incumbent LEC's artificially low tandem-switched transport rates;[235] and (8) the unitary rate structure hurts incumbent LECs because the unrecovered costs of the excess mileage are contained in the TIC, making the incumbent LEC's usage-based switched access charges less competitive.[236] AT&T additionally argues that rate shock will not be a problem if prices are set to TELRIC.[237]

59. In addition, SNET argues that AT&T's purported competitive advantage based on the locations of its inherited POPs has been mitigated substantially by the widespread availability of collocation and the presence of many alternative transport providers.[238] Ameritech and U S West state that, even if the Commission mandates the three-part rate structure, it would be too costly to relocate tandems inefficiently to increase transport revenue. Instead, tandems are located to maximize overall network efficiency, generally by placing

---

229 AT&T Comments at 59-60; Ameritech Reply at 29; BellSouth Comments at 73; SWBT Comments at 14, 64; U S West Comments at 59-60; Florida Commission Comments at 3.

230 AT&T Comments at 59-60; U S West Comments at 59-60.

231 AT&T Reply at 33.

232 BA/NYNEX Comments at 41; Ameritech Reply at 31; SWBT Reply at 15.

233 BA/NYNEX Reply at 36-37.

234 U S West Reply at 30-31.

235 BA/NYNEX Reply at 36-37; *see also* ALTS Comments at 22; Teleport Comments at 14, Reply at 11-12.

236 BA/NYNEX Reply at 37.

237 AT&T Reply at 32.

238 SNET Reply at 29-31.

them near high concentrations of end users and carriers.[239] Inefficient tandem placement would also affect the incumbent LEC's own routing of intraLATA toll and local traffic.[240]

60. CAPs and CLECs generally support the three-part rate structure, arguing that (1) distance-sensitive charges should be based on actual miles, rather than airline miles, reflecting actual LEC network efficiencies or inefficiencies;[241] (2) the unitary rate structure is not cost-based and inhibits competition;[242] and (3) the unitary rate structure discriminates against direct-trunked transport users by allowing tandem-switched transport users to purchase dedicated transport facilities in connection with tandem-switched transport at prices unavailable to others.[243] In addition, Teleport states that, unlike direct-trunked transport, tandem-switched transport is not a single service and does not use a single transmission pathway. Users of tandem-switched transport pay two switching charges and should therefore pay the cost of reaching each switch.[244]

61. Some commenters state that, because tandem-switched transport facilities are sized to handle peak-load overflow traffic from large IXCs that otherwise use direct-trunked transport facilities, some costs of tandem-switched transport should properly be imposed on direct-trunked transport customers.[245] SWBT opposes this argument, noting that, such a service-specific charge would drive users of direct-trunked transport to alternate providers, driving up the rates for small IXCs that remain.[246] SWBT supports recovery of some tandem-switching costs from a competitively neutral public policy element.[247]

62. TCI supports a rate structure that unbundles the components of tandem-switched transport and permits purchase of needed components from the lowest-cost supplier.[248] TCI

---

[239] Ameritech Reply at 29-30; U S West Reply at 30-31.

[240] Ameritech Reply at 29-30.

[241] ALTS Reply at 22.

[242] ALTS Reply at 22; Teleport Comments at 13-14.

[243] Teleport Comments at 13.

[244] Teleport Reply at 8.

[245] ACC Long Distance Comments at 14-15; Telco Communications Group Comments at 6-7.

[246] SWBT Comments at 63, Reply at 15.

[247] SWBT Comments at 63.

[248] TCI Comments at 15, Reply at 12.

states that the costs of the dedicated SWC-to-tandem link are NTS, and should be recovered on a flat-rated basis.[249] TCI states, however, that the costs of the common transport EO-to-tandem link vary, not with minutes of use, but with the trunk capacity attached to the tandem, sized as necessary to carry peak traffic levels.[250] Therefore, the costs of this common transport should also be recovered as a flat rate, capacity-based charge tied to the proportion of dedicated transport the IXC has provisioned on the SWC-to-tandem link.[251] TCI explains that this structure: (1) would be administratively more simple and efficient than the current structure; and (2) would reflect, more accurately than the current system, the costs of providing tandem-switched transport by automatically allocating to overflow users the costs of the peak capacity made necessary by the overflow traffic.[252] TCI would base these charges on airline mileage between the EO and the SWC as a check on the incumbent LEC's ability to choose routing that either increases IXC costs, or discriminates between its own IXC affiliate and unaffiliated IXCs.[253]

63. With respect to the tandem switch itself, MCI supports establishment of a combination of flat-rated and usage sensitive charges, stating that the tandem switch and the local switch are not substantially different and therefore should have the same rate structure. Many commenters state that the dedicated trunk port on the SWC side of the tandem should be priced on a flat-rate basis and charged to the user of the dedicated trunk because these costs are incurred in an NTS manner.[254] BellSouth disagrees with this position, however, stating that there are minimal NTS costs associated with tandem switching and arguing against mandatory disaggregation of tandem switching costs into NTS and TS components. BellSouth, instead, argues in favor of LEC flexibility to disaggregate as they wish.[255]

64. For many of the same reasons as those opposing a peak and off-peak rate structure for the local switch, several commenters state that they oppose a mandatory peak

[249] TCI Reply at 13.

[250] TCI Comments at 16, Reply at 13.

[251] TCI Comments at 16, Reply at 13-14.

[252] TCI Comments at 16, Reply at 13-14.

[253] TCI Comments at 17, Reply at 14-15.

[254] AT&T Comments at 60, Reply at 33; Ameritech Comments at 20; SWBT Comments at 13-14; Teleport Comments at 19-20, Reply at 11-12.

[255] BellSouth Comments at 73.

rate structure for tandem-switched transport.[256] These commenters primarily state that: (1) peak rate pricing would have a *de minimis* impact on the usage patterns and incumbent LEC network design decisions because less than 15% of the BOC interstate traffic is access;[257] and (2) it would be impossible to determine peak and off-peak hours with any degree of certainty or consistency because peak hours vary with the region of the country, type of service, type of user, rate zone, and other factors.[258]

65. Several commenters suggest that LECs should have the flexibility to implement a peak rate structure on a permissive basis.[259] The Texas Commission states that peak and off-peak pricing would allow the LEC to recover a portion of the larger tandem switching capacity necessitated by overflow traffic from large IXCs.[260] The Georgia Commission indicates that the peak rate structure should be optional for both LECs and their customers, and that LECs should not be permitted to offer peak and off-peak pricing until after the proposals have received regulatory review and approval.[261] Excel states that tandem switching services, like local switching, should be subject to peak and off-peak pricing.[262]

66. Teleport states that the Commission could achieve the economic efficiency benefits of a peak rate structure without resorting to time-of-day pricing by establishing a flat-rate pricing structure for the tandem switch, without disaggregating the costs into TS and NTS components. Teleport supports the establishment of flat-rated port charges as reflective of the way LECs incur the costs of dedicated tandem trunk ports. According to Teleport, however, the Commission should carefully examine the portion of tandem switching cost that is arguably TS to determine whether the costs of separate measurement and billing merit the development of separate rate elements for those costs. According to Teleport, tandem switch ports are purchased to provide the purchaser with the ability to place a certain amount of traffic on the switch at its peak period; a flat-rate tandem-switching charge tied to port capacity would therefore reflect the costs of the tandem switch, which is sized to handle peak

---

[256] MCI Comments at 85-86; AT&T Comments at 60, Reply at 33; Cable & Wireless Comments at 17; CompTel Comments at 28; SWBT Comments at 63; U S West Comments at 60.

[257] CompTel Comments at 28.

[258] CompTel Comments at 28; SWBT Comments at 63.

[259] *E.g.*, Ameritech Comments at 19; BellSouth Comments at 73; Georgia Commission Reply at 27; Texas Commission Comments at 16-17.

[260] Texas Commission Comments at 16-17.

[261] Georgia Commission Reply at 27.

[262] Excel Comments at 13.

load traffic.[263]

67. Several commenters request that we update our tandem switched transport rate structure to include the cost of appropriate multiplexing equipment used providing tandem-switched transport.[264]

b. Rate Levels

68. *Allocation of 80 percent of the tandem switching revenue requirement to the TIC.* Both incumbent LECs and CAPs support reallocation from the TIC to tandem switching rates the 80% of tandem switching costs currently recovered through the TIC.[265] Ameritech states that the Commission should accomplish this reallocation by increasing the price cap indices for tandem-switched transport to reflect the full amount of the tandem costs. Ameritech states that this action would be consistent with the Court's remand of the *CompTel* case.[266] Sprint, on the other hand, opposes allocating TIC costs to transport rates, but instead favors setting all rates for transport facilities at TELRIC-based prices within five years.[267]

69. *SS7 signalling costs.* BellSouth states that tandem rates should be revised downward to reflect removal of the 20% of the CCS/SS7 charge that was assigned to the tandem and, at the same time, all CCS/SS7 costs should be assigned to new, signalling rate elements.[268]

70. *Overhead loadings on the tandem-switch.* Cable & Wireless states that, in this proceeding, the Commission should equalize the overhead loading factors for all transport options by directing that the difference in transport rates is equal to the difference in the LRIC of each option (DS3, DS1, and TST). In doing so, the Commission would (1) ensure that all access customers pay the same dollar amount of overhead per unit of traffic; and (2) increase the competitive neutrality of the rate structure.[269] The Commission, in contrast,

[263] Teleport Comments at 19-20, Reply at 11-12.

[264] USTA Comments at 60; GTE Reply at 24.

[265] Ameritech Comments at 18-19; BellSouth Comments at 74; U S West Comments at 65; ALTS Reply at 22; Teleport Comments at 18.

[266] Ameritech Comments at 19.

[267] Sprint Comments at 26.

[268] BellSouth Comments at 74.

[269] Cable & Wireless Comments at 19.

should not provide for an equal percentage of overhead per unit cost of transport because doing so would place small IXCs, which use proportionately more TST, at a disadvantage.[270]

71. WorldCom also supports LEC cost studies that would be used to justify reinitialization of tandem switching rates.[271] WorldCom states that we should use the "lowest of the low" methodology in order to ensure that the incumbent LECs do not discriminate unreasonably in the allocation of overheads (or, for TSLRIC/TELRIC studies, the allocation of forward-looking common costs). Under this methodology, the Commission would require the incumbent LECs to demonstrate that the allocation of overhead loadings or common costs to the tandem switching rate is no greater than the allocation of overhead loadings or common costs to the comparable transport service to which the lowest amount of overhead or common costs have been allocated.[272] The Commission, in enforcing this requirement, could examine the allocation of overheads or common costs to both tandem switching an other specific transport services.[273]

72. CompTel argues that the Commission should prescribe TSLRIC rates for all access services.[274] Recognizing that a "flash-cut" to TSLRIC rates may be infeasible for all access charges, CompTel states that the Commission should establish priorities, prescribing TSLRIC rates first for those access elements that are least subject to the market discipline of competition. In allocating common costs, CompTel argues that the Commission should adopt a "reverse Ramsey" pricing method. Under this method, CompTel argues that we should allocate a relatively small portion of common costs to those access elements that are least subject to competitive market forces, while maintaining access rate elements that may be subject to competitive pressures at current levels for the present.[275]

73. *Use of weighted average DS3/DS1 rates and 9000 minutes of use per month assumption.* AT&T and other commenters state that the Commission should set rates for tandem switching and tandem-switched transport transmission facilities at TELRIC levels

---

[270] *Id.*

[271] WorldCom Comments at 55.

[272] WorldCom Comments at 55-56.

[273] WorldCom Comments at 56.

[274] CompTel Comments at 16; *see also* American Communications Services, Inc. Reply at 20-21 (advocating reinitialization of tandem switching rates based on the *Local Competition Order* proxy of $0.0015 per minute).

[275] CompTel Comments at 17.

established by state commissions in accordance with the *Local Competition Order*.[276] These commenters state that use of TELRIC rate levels will make the benchmark DS3 to DS1 benchmark ratios unnecessary.[277]

74. Many commenters state that the Commission should no longer require carriers to assume 9000 minutes of use per month when setting per-minute rates for shared transport circuits.[278] Some of these commenters favor the use of actual minutes of use.[279] ALLTEL, for example, states that it estimates the usage of tandem-switched trunks at approximately 4000 MOU per month.[280] U S West favors retaining the 9000 minute of use assumption, but permitting LECs to develop its own unique conversion factor if it so chooses.[281] Sprint, in contrast, states that the 9000 MOU assumption is reasonably attainable because the use of tandem-to-EO circuits is largely within the LEC's control.[282] If the LEC chooses to provision these facilities so as to obtain a lower utilization, the LEC's access customers should not bear the costs of this decision.[283] Similarly, if the IXC wishes to order additional facilities, it should be permitted to do so at an additional cost.[284]

75. *Relationship with market based/prescriptive approach.* Sprint opposes any premature relaxation of the Commission's rate structure rules, arguing instead that the market-based approach gives incumbent LECs too much pricing flexibility too soon.[285] Sprint notes, however, that the Commission should permit density-based deaveraging of direct-trunked transport rates immediately.[286] According to Sprint, because there is a much greater demand for special access in high-density areas than there is in low-density areas, direct-trunked

[276] AT&T Comments at 59; CompTel Reply at 3;

[277] AT&T Comments at 59.

[278] U S West Reply at 32; ALLTEL Comments at 12-13; GVNW Comments at 7, Reply at 7-8; Harris, Skrivan & Associates Comments at 6; Minnesota Independent Coalition Comments at 16.

[279] *E.g.*, GVNW Reply at 7-8; Harris, Skrivan & Associates Comments at 6.

[280] ALLTEL Comments at 12-13.

[281] U S West Reply at 32.

[282] Sprint Comments at 27.

[283] Sprint Comments at 27.

[284] Sprint Comments at 27.

[285] Sprint Comments at 27.

[286] Sprint Comments at 28-29.

transport rates, which are based on special access rates, understate the true cost of direct-trunked transport in less dense areas.[287] Geographic deaveraging of these rates would allow LECs to establish cost-based rates in each density zone.[288]

D. Transport Interconnection Charge (TIC)

76. The issues presented by the existence of the TIC generated substantial comment from all segments of the telecommunications industry. The comments are organized below into three broad groups: (1) causes and possible reassignment of sums in the TIC; (2) approaches that rely on market forces to address any amounts remaining in the TIC after some amounts are reallocated; and (3) approaches that would eliminate or phase out some or all of the TIC.

1. Causes and possible reassignment of amounts in the TIC

77. *General.* USTA and incumbent LECs assert that, to the extent TIC costs can be identified and attributed to specific services, those costs should be recovered from those services.[289] Minnesota Independent Coalition, however, argues that costs that may be easily identifiable and correctable for large LECs may not be for small LECs.[290]

78. Time Warner argues that the TIC was explicitly designed to make all IXCs pay for tandem-switched transport even though some IXCs only use the tandem switch for overflow traffic. According to Time Warner, the TIC distorts competition for switched transport service, and it should not be a surprise that little competition has developed there.[291] Time Warner argues that the Commission must require that the costs associated with the TIC are paid by cost causers and recovered in the manner in which they are incurred, which will require substantial revision to the TIC. Accordingly, Time Warner argues that those costs that can be reasonably attributed to other elements must be so assigned, and that this approach is

---

287 Sprint Comments at 28-29.

288 Sprint Comments at 28-29.

289 *See, e.g.,* USTA Comments, Attachment 10 at 9; PacTel Comments at 6; BA/NYNEX Comments at 36-37; Aliant Comments at 2; SNET Reply at 27-28; Frontier Comments at 9; ALLTEL Reply at 8; TCA Comments at 4; Minnesota Independent Coalition Comments at 17; Alaska Telephone Association Comments at 9; Harris, Skrivan & Associates Comments at 6.

290 Minnesota Independent Coalition Comments at 17.

291 Time Warner Comments at 12-13.

most consistent with *CompTel v. FCC*.[292] TRA also supports the identification of cost misallocations and other practices that cause costs to be assigned to the TIC and reassigning such costs to various access services and other nonregulated activities, as appropriate.[293]

79. ALTS and ACSI contend that the Commission should quantify and eliminate all readily correctable cost misallocations in its current access tandem switching regime.[294] Teleport also favors an approach in which obvious misallocated costs are reallocated. Teleport, however, would require incumbent LECs to produce for public review a complete report of the costs currently included in switched access and the proportion and type of costs assigned to the TIC. Until this report is analyzed, it will not be possible to identify whether the TIC contains truly "lost" costs, or, rather, costs that have "conveniently" been placed in the only switched access rate element immune from competition.[295]

80. Some consumer groups and consumer advocates recommend identifying misallocated costs and moving them to the appropriate cost element.[296] State Consumer Advocates believe that all remaining costs represent a portion of joint and common costs and should be recovered by increasing all of the transport rate elements.[297]

81. Several state commissions also agree that costs should be reallocated. The Washington Commission is in favor of eliminating the TIC and reassigning costs according to causation. The Washington Commission states that it has eliminated the state equivalent of the TIC, finding that there was no need for it once the company's other transport and switching rates were set to provide appropriate revenue levels.[298] In a similar manner, the Illinois Commission argues that embedded costs currently recovered by the TIC should be reassigned to other rate elements to the extent cost causation can be established, and the incumbent LECs should be given any additional flexibility needed to raise prices within the price cap framework for those rate elements to which costs have been reassigned. The Illinois

[292] Time Warner Comments at 12-13.

[293] TRA Comments at 36.

[294] ALTS Comments at 26; ACSI Reply at 21.

[295] Teleport Comments at 30-32.

[296] *See, e.g.*, AARP, *et al.*, Comments at 17; Texas Public Utility Counsel Comments at 16; State Consumer Advocates Comments at 36.

[297] State Consumer Advocates Comments at 34-37.

[298] Washington Commission Comments at 7.

Commission believes that the entire TIC can be reallocated in this manner.[299] The Georgia Commission states that the FCC must (1) verify the costs that have been loaded onto the TIC; (2) verify the amount of those costs that should be recoverable on a going-forward basis and ensure that the unrecovered amounts resulted purely from regulatory restriction, not competitive pressures; and (3) conduct any restructuring in order to establish cost-based rates that avoid anticompetitive pricing.[300] The Ohio Commission argues that only after incumbent LECs have demonstrated the cost amounts currently in the TIC should any costs be reallocated to tandem switching. In addition, the Ohio Commission states that it is up to state commission to decide how the intrastate portions of TIC-related charges should be recovered.[301]

82. On the other hand, several parties argue that not all costs should be reallocated. Sprint, for example, argues that revenue requirements other than the TELRIC of tandem switching that are assigned to the TIC under current rules should be left in the TIC and phased out.[302] WorldCom asserts that incumbent LEC allegations as to the "costs" of common transport recovered through the TIC are incorrect. WorldCom states that to truly reset transport rates based on costs would require a forward-looking cost study to reinitialize rates for both common and dedicated transport and that mere shifting of TIC costs to other rate elements is inadequate.[303] WorldCom also argues that rates based on forward-looking costs will not be revenue neutral, and incumbent LECs should not be guaranteed recovery of all residual costs.[304]

83. Several parties address the possible relationship of the TIC to universal service. WITA argues that the TIC is an implicit support mechanism for rate-of-return LECs that should be included in the federal universal service support mechanism for rate-of-return LECs.[305] The Texas Public Utility Counsel argues that increased levels of universal service support should be used to offset the amount of the TIC that is earmarked for phase-out.[306] Time Warner, on the other hand, argues that the Commission should not attempt to transfer

---

[299] Illinois Commission Comments at 12-13.

[300] Georgia Commission Comments at 32.

[301] Ohio Commission Reply at 5-6.

[302] Sprint Reply at 18.

[303] WorldCom Reply at 34.

[304] WorldCom Reply at 38.

[305] WITA Comments at 8.

[306] Texas Public Utility Counsel Comments at 21.

costs currently recovered through the TIC to universal service because there is no evidence supporting such a decision. Such a decision would be inconsistent with the Joint Board's recommendation that universal service funding should be determined on a forward-looking cost basis.[307]

84. Several parties address the need to adjust PCIs and SBIs if reallocation of TIC costs are permitted or required. BellSouth and BA/NYNEX, for example, state that if the Commission authorizes reassignment of TIC costs, it must permit incumbent LECs to adjust the TIC SBI and other relevant SBIs to ensure they have an opportunity to recover the reassigned costs.[308] In a similar vein, Aliant advocates exogenous cost increases for specific service categories in the trunking basket so that incumbent LECs can recover TIC costs to the extent the market permits.[309]

85. *Tandem Switching Costs.* USTA and the majority of the incumbent LECs assert that the tandem switching revenue requirement being recovered through the TIC should be reassigned and recovered through tandem switching rates.[310] USTA estimates this component of the TIC to be $400 million, or 12.93% of total industry TIC revenues.[311] Ameritech contends that this reassignment would be consistent with *CompTel v. FCC* and would allow incumbent LECs to increase their tandem switching rates to economically rational levels given available market substitutes.[312] NECA states that the tandem-switching costs currently assigned to the TIC can be identified and could be assigned to the tandem-switching rate element, thereby reducing the TIC and increasing tandem-switching revenue for NECA traffic-sensitive pool members by $15.1 million.[313]

86. Cable & Wireless contends that 80 percent of the interstate tandem switching *revenue requirement* was allocated to the TIC, as distinguished from interstate tandem switching *costs*. Cable & Wireless asserts that state commissions have found that the incumbent LEC's LRIC of tandem switching is far below even the 20 percent rate that the

[307] Time Warner Comments at 15; Time Warner Reply at 21-22.

[308] BellSouth Comments at 81 n.141; BA/NYNEX Comments at 37.

[309] Aliant Comments at 3.

[310] *See, e.g.*, USTA Comments at 61; BellSouth Comments at 75; GTE Comments at 36; PacTel Comments at 71; SWBT Comments at 9-10; Citizens Utilities Comments at 31; ALLTEL Comments at 13; Puerto Rico Tel. Comments at 17; Roseville Tel. Comments at 11-12; Sprint Comments at 28.

[311] USTA Comments, Attachment 11.

[312] Ameritech Comments at 18-19.

[313] NECA Comments at 5 n.15.

Commission set and that it is therefore doubtful that any of the TIC should be allocated to tandem switching on a forward-looking cost basis.[314] Cable & Wireless alleges that the tandem-switching revenue requirement consists, in large part, of overhead and subsidies placed on tandem switching during the "equal charge" era. Cable & Wireless asserts that the Commission should not ignore actual cost data showing tandem-switching costs to be far less than the revenue requirement indicates.[315]

87. Sprint urges that the Commission not reassign the balance of the tandem switching revenue requirement from the TIC to the tandem switching rate element. It contends that a tandem switching rate that recouped the entire revenue requirement might reduce tandem switching revenues for incumbent LECs because these rates would be so high that the use of tandem switching would be uneconomic for IXCs. In addition, Sprint asserts that the existing tandem switching rates reflect a much higher than reasonable allocation of overhead costs. The tandem switching rate should, according to Sprint, be based on TELRIC costs and should be similar to today's tandem switching charges.[316]

88. *SS7 costs.* USTA and incumbent LECs contend that the Commission should identify the portion of the tandem revenue requirement that recovers the costs of SS7 signal transfer points ("STPs") and the costs of the links between service switching points ("SSPs") and STPs. These costs are associated with providing FGD service and are currently recovered as part of the TIC. USTA asserts that they should be recovered through existing SS7 rate elements.[317] USTA estimates this component of the TIC to be $58.7 million, or 1.89 percent of total industry TIC revenues.[318] BellSouth asserts that the FCC should remove from the TIC the portion of common channel signaling costs that are booked to Category 2 tandem switching and that these costs should be recovered through new rate elements.[319] U S West argues that the costs associated with SS7 signalling should be recovered through transport charges.[320]

---

[314] Cable & Wireless Comments at 20.

[315] Cable & Wireless Comments at 21.

[316] Sprint Reply at 18.

[317] *See, e.g.*, USTA Comments at 61; GTE Comments at 36; SWBT Comments at 9-10; Citizens Utilities Comments at 31; NECA Comments at 7-8.

[318] USTA Comments, Attachment 11.

[319] BellSouth Comments at 75-76.

[320] U S West Comments at 65.

89. *Tandem-Switched Transport Transmission Rate Setting.* Most incumbent LECs support a modified tandem-switched transport transmission rate structure that includes: (1) assessment of the SWC-to-access tandem portion as dedicated transport (which includes the cost of DS3/DS1 multiplexing at the tandem office) measured from the SWC to the access tandem; (2) assessment of the access tandem-to-end office portion as tandem-switched transport measured from the access tandem to end office; and (3) the assessment of a multiplexer charge between the access tandem and end office. Incumbent LECs generally assert that the TIC includes the costs of the Commission having adopted a less efficient interim transport rate structure. USTA and incumbent LECs argue that the rates for tandem-switched transport transmission must be increased to reflect the costs of this revised rate structure, thereby shifting costs from the TIC.[321] According to USTA, these changes will result in rates that more accurately capture a LEC's actual costs of providing tandem-switched transport service.[322]

90. Many incumbent LECs also argue that the 9000 MOU assumption should be eliminated in favor of actual MOU levels, contending that actual usage is far less than 9000 MOUs. Among the estimates of actual usage are: U S West, 5700;[323] NECA, approximately 4500;[324] GTE, 5300;[325] and ALLTEL, approximately 4000.[326] NECA states that it would develop a MOU figure that more closely corresponds to the actual rural, low-usage characteristics of its traffic-sensitive pool members, and base its tariff rates on that figure.[327] Minnesota Independent Coalition asserts that the assumed monthly usage of 9000 MOU per transport circuit is unrealistic for low volume, rural routes.[328]

91. WorldCom asserts that actual fill factors, in MOUs per month, on a given transmission facility, are irrelevant; rather, the fill factors that would represent efficient network deployment are far more relevant.[329]

---

[321] *See, e.g.,* USTA Comments at 60; BellSouth Comments at 77; Citizens Utilities Comments at 31-32.

[322] USTA Comments at 60.

[323] U S West Comments at 66-67.

[324] NECA Comments at 8 n.22.

[325] GTE Comments at 38.

[326] ALLTEL Comments at 12-13.

[327] NECA Comments at 8 n.22.

[328] Minnesota Independent Coalition Comments at 16.

[329] WorldCom Reply at 35.

92. *Host-Remote Trunking Rate*. USTA and incumbent LECs state that for service to a remote switch, the tandem-switched transport transmission fixed and per mile/per MOU charge applies for transport between the host and remote switch, but that only a portion of the host/remote revenue requirement is recovered through these rates. They state that the difference is included in the TIC. USTA argues that the costs specific to host/remote transport that are in the TIC should be included in the tandem-switched transport rates because those rate elements are currently applied to host/remote connections.[330] USTA estimates this component of the TIC at $160.5 million, or 5.17 percent of total TIC revenues.[331]

93. NECA submits that incumbent LECs install host-remote facilities because these facilities are cheaper than installing a separate end office switch at the remote location. Because the host-remote transport facilities are not dedicated to any particular user, NECA contends that the costs should be removed from the TIC and assigned to the local switching element.[332] NECA states that assigning these revenues, instead, to the costs of tandem-switched transport would disproportionately raise tandem switched transport rates.[333]

94. *DS1/voice-grade multiplexer costs.* USTA and incumbent LECs state that analog switches do not have direct DS1 interfaces and, as such, require a combination of trunk unit ports and a DS1/voice grade multiplexing function to take the traffic to the DS0 level to be switched. Incumbent LECs state that in the analog switching environment, the costs of multiplexing from the DS1 to DS0 level have been assigned primarily to transport, while in the digital switching environment, this function is incorporated in the switch and is assigned to local switching. They assert that the costs of these analog multiplexers were not included in the special access formulas used to derive switched transport rates and are thus included in the TIC. USTA contends that these analog multiplexer costs should be associated with the switching function and assigned to the Local Switching category.[334] NECA states that assigning analog multiplexing costs to the local switching rate element would make the assignment of analog multiplexing costs consistent with the assignment of costs associated

[330] *See, e.g.*, USTA Comments at 61-62, Attachment 10 at 4; BellSouth Comments at 77; U S West Comments at 65-66; Citizens Utilities Comments at 32; GTE Comments at 37; Minnesota Independent Coalition Comments at 16.

[331] USTA Comments, Attachment 11.

[332] NECA Comments at 6.

[333] NECA Comments at 6 n.18.

[334] *See, e.g.*, USTA Comments at 62; BellSouth Comments at 77-78; PacTel Comments at 71; U S West Comments at 66; GTE Comments at 36.

with this function in digital switches.[335] USTA indicates that analog switches account for approximately 25 percent of the RBOC lines in service.[336] USTA estimates the "Analog End Office Trunk Switch Ports" component of the TIC at $138.4 million or 4.46 percent of total TIC revenues.[337]

95. Cable & Wireless asserts that the costs of analog multiplexers are imposed by direct-trunked transport customers; therefore the costs should be built into the direct-trunked transport rate elements, or a separate DS1:DS0 multiplexing element should be added for direct-trunk transport customers.[338]

96. *Use of special access rates to establish Direct-Trunked Transport Rates.* USTA and many incumbent LECs contend that the TIC results in large part from the fact that the transport rate restructure order repriced switched transport services based on special access high-cap rates despite the fact that, in the past, switched access and special access rates were derived very differently.[339]

97. USTA explains that the local transport equal charge rates were derived from a revenue requirement that was the result of the Commission's Part 36 and 69 cost allocation rules on investments and expenses. This mandated cost allocation process predominantly used general categorizing and averaging of costs across geographic areas, technologies, services, and jurisdictions.[340] Plant investment was the primary driver because expenses generally followed the allocation of the plant. Because there were basically only two rate elements for switched local transport (the per-minute termination charge and the per-minute facility charge), the rates could deviate very little, if at all, from the rate levels resulting from the cost allocation rules. Special access rates, on the other hand, were more heavily based on a unit investment approach which more specifically identified the actual plant used for each service. The unit investments were then used as a basis for loading overheads. In addition, under the cost allocation process, high capacity facilities could be directly assigned to the special access

---

[335] NECA Comments at 5-6.

[336] USTA Comments, Attachment 10 at 9. *See also* ARMIS 43-07.

[337] USTA Comments, Attachment 11.

[338] Cable & Wireless Comments at 21. *See also* Citizens Utilities Comments at 32 (supporting assignment to direct-trunked transport).

[339] *See, e.g.*, USTA Comments at 62-65; BellSouth Comments at 80; GTE Comments at 38.

[340] *See, e.g.*, GTE Comments at 38; Citizens Utilities Comments at 32.

category.[341]

98. USTA therefore asserts that when the transport rate restructure set switched transport rates based on special access rates, the TIC represented the difference in revenues between the two pricing schemes and the differences in the costing methodologies used for each service in the past. The TIC, therefore, represents the averaging of costs across technologies, geographies, services, and jurisdictions that were inherent in the old cost allocation rules that determined the equal charge rates.[342] According to USTA, a detailed direct cost approach demonstrates that the cost allocation rules assign more investment to transport than is actually used in providing the service. The difference in costs is currently in the TIC, even though the costs are actually incurred to provide local services, intrastate services, and/or interstate services other than local transport.[343] USTA estimates this "transport averaging, cost allocations, and cost recovery" component of the TIC at $1.16 billion, or 37.27 percent of the total TIC revenues.[344]

99. USTA and incumbent LECs argue that changes to this structure will require Joint Board action, and that until such action can be taken, these TIC components should be removed from the per-MOU TIC rate and should be bulk-billed to IXCs based on interstate revenues or minutes.[345]

100. USTA alleges that part of the TIC also represents circuit equipment and cable and wire facilities serving longer haul traffic that have an embedded Part 36 cost many times greater than that based on a special access costing methodology. According to USTA, the cost of hauling traffic to scattered local switches in remote areas is much greater than that of hauling the same amount of traffic in larger cities at special access rates. The cost difference is part of the TIC.[346] Citizens Utilities argues that circuit termination costs could be directly assigned for jurisdictional purposes, but that Part 36 requires that circuit equipment be allocated to categories based on average cost per termination.[347] USTA estimates that the investment in interexchange cable and wire is $37.4 million, or 1.21 percent of the total TIC

---

[341] USTA Comments at 63-64.

[342] USTA Comments at 63-64.

[343] USTA Comments at 65.

[344] USTA Comments, Attachment 11.

[345] USTA Comments at 66.

[346] *See, e.g.*, USTA Comments at 65; BellSouth Comments at 80; GTE Comments at 38.

[347] Citizens Utilities Comments at 33.

revenues.[348]

101. U S West contends that the cost of interexchange facilities per unit of traffic in sparsely populated areas is several times more than the cost of exchange facilities in densely populated areas. U S West argues that this is part of the reason why special access is less expensive per unit of traffic than transport, and accounts for most of the TIC not attributable to other factors listed in U S West's comments.[349] NECA argues that many of its pool participants do not have high-capacity DS1 or DS3 special access services throughout their service areas because they have no customers that require these services. NECA submits that the areas without demand for DS1 or DS3 special access services have higher transport costs than those areas that do have these services. NECA suggests that the Commission discontinue its reliance on special-access transport rates as a surrogate for local transport costs; NECA would then develop cost-based transport rates and file them in access tariffs.[350] Aliant asserts that a significant portion of the TIC results from the fact that special access is primarily an urban service while switched transport is primarily a rural service. Aliant states that approximately 77 percent of Aliant's DS1 special access revenue is located in Lincoln, Nebraska, while 79 percent of Aliant's tandem-switched transport and 58 percent of Aliant's DS1 direct-trunked transport revenue is located outside of Lincoln.[351]

102. Cable & Wireless argues that special access is generally less costly than direct-trunked transport because special access, unlike direct-trunked transport, generally is limited in use to low-cost urban areas. Cable & Wireless contends that the additional costs of direct-trunked transport should be removed from the TIC.[352]

103. *Central Office Equipment Maintenance Expenses.* USTA and incumbent LECs argue that the Part 36 and Part 69 rules overstate the assignment of COE maintenance expenses to the TIC.[353] USTA states that by separating COE maintenance expenses on the basis of the combined COE investment, a mismatch occurs to the extent that the expenses associated with maintaining the investment are apportioned differently than the investment being maintained. This results in a portion of COE maintenance expense for local and

[348] USTA Comments, Attachment 11.

[349] U S West Comments at 69-70.

[350] NECA Comments at 7.

[351] Aliant Comments at 3.

[352] Cable & Wireless Comments at 21-22.

[353] *See, e.g.,* USTA Comments at 62-63; BellSouth Comments at 78; U S West Comments at 68-69; Citizens Utilities Comments at 33; GTE Comments at 38.

operator switches being allocated in Part 69 to Common Line, Transport, and Special Access, where there is no switch investment to maintain.[354] USTA estimates COE Maintenance Misallocations at $101.8 million, or 3.28 percent of the TIC.[355] According to USTA, a more cost-causative approach would be to separate the central office expenses based on the separation of the investment being maintained.[356]

104. To accomplish this modification, USTA proposes to modify sections 36.321 and 69.401(b).[357] USTA states that COE switching expenses should be assigned to the Transport elements based on a relationship of interstate tandem switching investment assigned to the Transport element to total Part 69 interstate switching investment, with the remainder being assigned to local switching. According to USTA, COE operator expenses should be assigned to information, interexchange and operator transfer elements based on the relative relationships from assignment of the operator investment to these elements. By using the above-described approaches, USTA states that costs will be removed from the common line, access and transport elements and will be reassigned to the switching element.[358] USTA claims, however, that these changes will require Joint Board action and, until such action can be taken, these TIC components should be removed from the per-MOU TIC rate and should be bulk-billed to IXCs based on interstate revenues or minutes.[359]

105. Cable & Wireless argues that, to the extent that these costs are not related to facilities-based transport, they should be moved out of the TIC and, to the extent that they are NTS, they should be recovered as part of the per-line or per-port local switching costs.[360]

106. *Use of Circuit Terminations in Separating Costs Between Private Line and Message Services*. USTA asserts that Part 36.126 assigns interexchange trunk investment to message joint, interstate private line, and intrastate private line categories and allocates these costs based on the average cost per circuit termination. USTA states that the costs in interexchange circuit equipment categories, except message joint, are jurisdictionally pure and could be directly assigned to jurisdictions if it were permitted by the Part 36 Rules. For the

[354] BellSouth Comments at 78.

[355] USTA Comments, Attachment 11 at 1.

[356] USTA Comments, Attachment 10 at 7.

[357] USTA Comments, Attachment 10 at 7.

[358] USTA Comments, Attachment 10 at 8.

[359] USTA Comments at 62-63.

[360] Cable & Wireless Comments at 22.

message joint investment classification, traffic usage factors determine the final jurisdictional allocation. USTA states that the distribution of costs to categories and jurisdictions based on direct identification would reduce the TIC by reassigning costs to intrastate and interstate.[361] USTA estimates that the use of circuit Termination Counts misallocates $630.66 million to the TIC, or 20.33 percent of the TIC.[362]

107. Frederick & Warinner argues that differences in the definition of circuit terminations when allocating costs between switched and special access contribute to the TIC, resulting in costs being over-allocated to message trunking facilities and under-allocated to special access. Frederick & Warinner proposes an "equivalent termination count" be used for message circuit equipment in COE Category 4.23 in order to more appropriately reflect how CO transmission costs are incurred.[363] Frederic & Warinner generated an "equivalent termination count" based on the ratio of tariffed rates. Using the ratio of NECA's DS1 channel termination rate to the DS0 channel termination rate gives a weighting of 5.2. According to Frederick & Warinner, changing terminations in this way would (1) allocate more costs to special access and less to switched access; (2) bring special access rates closer to those determined by LRIC cost studies; (3) reduce the message toll costs being allocated to various transport elements; and (4) increase the tandem-switched termination rate (using special access rates divided by assumed MOU), thereby reducing the revenue requirement to be collected in the TIC.[364]

2. Market-Based Approaches

108. The incumbent LECs generally support continued recovery of all remaining sums in the TIC after reassigning any identifiable TIC costs to other services. USTA and incumbent LEC parties state that, to a large extent, the TIC reflects costs that the separations and access charge rules assign to interstate local transport.[365] While USTA and incumbent LEC parties state that it is possible to identify the cause of only a portion of the costs included in the TIC,[366] this does not suggest that only a portion of the TIC should be

[361] USTA Comments, Attachment 10 at 6; BellSouth Comments at 78-79; U S West Comments at 67-68; Citizens Utilities Comments at 33.

[362] USTA Comments, Attachment 11 at 1.

[363] Frederick & Warinner Comments at 8-9.

[364] Frederick & Warinner Comments at 10.

[365] *See, e.g.*, USTA Comments at 59.

[366] *See, e.g.*, USTA Comments at 59; Sprint Comments at 28.

recovered in a post-access reform environment.[367] Ameritech asserts that a large part of the TIC contributes to the incumbent LECs' ability to maintain affordable basic exchange rates.[368] Incumbent LEC parties assert that the TIC represents actual costs that have been assigned to the interstate jurisdiction, and that companies are entitled to recovery of the amount currently assigned to the TIC.[369] Evans *et al.* submits that rate-of-return LECs are recovering jurisdictionally interstate, actual transport costs under the current system, and that any changes to the rate structure must allow continued recovery of the actual, defined revenue requirement.[370] Roseville Tel. states that the remaining TIC costs result from Part 36 rules and should be reassigned to the Interstate Special Access, Interstate Local Switching and intrastate jurisdictions.[371]

109. ALTS and ACSI argue that once readily-correctable misallocations are removed, market-based forces should be relied upon to reduce any remaining TIC.[372] Spectranet asserts that the need for a transition period applies as much to new entrants as it does for incumbent LECs because the immediate flash-cutting of access rates to LEC cost will undermine the basis upon which new entrants were planning to enter the local exchange business.[373]

110. Several parties allege that a Federal-State Joint Board pursuant to section 410(c) is required before the TIC can be fully eliminated. NARUC states that solving the TIC issue requires Joint Board action prior to action by the FCC.[374] USTA and incumbent LEC parties assert that many of the changes necessary to eliminate the TIC will require Joint Board action.[375] Frontier states that the FCC should promptly convene a Joint Board to address these

[367] USTA Comments at 58.

[368] Ameritech Reply at 32.

[369] *See, e.g.*, BA/NYNEX Reply at 39; PacTel Comments at 72; NECA Comments at 4 n.11; SNET Comments at 39-40; GVNW Comments at 8; Alaska Telephone Association Comments at 9; Western Alliance Comments at 21-22.

[370] Evans, *et al.*, Comments at 4.

[371] Roseville Tel. Comments at 11-12.

[372] ALTS Comments at 26; ACSI Reply Comments at 21.

[373] Spectranet Comments at 4.

[374] NARUC Comments at 7.

[375] *See, e.g.*, USTA Comments at 62-63; GTE Comments at 39.

issues on a schedule that coincides with the timetable for proposed phase-out of the TIC.[376] Until such action can be taken, these incumbent LEC parties argue that the remaining TIC components should be removed from the per-MOU TIC rate and should be bulk-billed to IXCs based on interstate revenues or minutes.[377] Ameritech asserts that the remainder of the TIC should be billed to interstate providers of telecommunications services in a competitively neutral manner on a flat-rate basis.[378] Roseville Tel. asserts that the remaining portion of the TIC should be recovered through a "Separations Cost" rate element, at least until a Joint Board reforms the separations rules. Roseville Tel. states that this will allow recovery of properly-incurred costs by an explicit mechanism applied equally to all cost-causers (i.e., users of interstate access services).[379] NECA and TDS contend that incumbent LECs should continue to collect the balance of the TIC through a smaller TIC-type charge or through alternative collection arrangement such as bulk-billing. They state that this charge would continue to be collected pending Joint Board action to change the separations rules.[380]

111. BA/NYNEX states that there are two interim solutions to sums remaining in the TIC pending separations changes. First, residual TIC amounts could be recovered from IXCs based on their proportionate share of LEC interstate access minutes. Second, LECs could recover any residual TIC on a per-presubscribed line basis to the IXCs. For price cap purposes, any TIC residual should be in the trunking basket and LECs should be allowed to target price cap reductions to this element. Pending separations changes, these mechanisms would be easy to administer, would not unduly burden the IXCs and would enable the LEC to reduce the amounts at issue through targeting of price cap reductions.[381] BA/NYNEX asserts that the remaining costs recovered through the TIC are primarily NTS and, therefore, should be recovered through a flat-rate charge. According to BA/NYNEX, such flat rate charges would resemble the charges states have adopted for UNEs, would reduce the arbitrage problem, because incumbent LECs would no longer have to charge high per-minute rates compared to the rates for UNEs, and would, when combined with the rates for local telephone lines and the EUCL charge, come close to the UNE rates for local loops and switches in

[376] Frontier Comments at 9 n.17.

[377] *See, e.g.,* USTA Comments at 62-63; PacTel Comments at 72; SNET Reply at 27-28; Alaska Telephone Association Comments at 9.

[378] Ameritech Reply at 32.

[379] Roseville Tel. Comments at 12.

[380] NECA Comments at 7; TDS Comments at 23-24.

[381] BA/NYNEX Comments at 38.

many instances.[382]

112. Several incumbent LECs propose specific mechanisms to recover any remaining TIC costs. U S West recommends that TIC costs that cannot be reassigned to other access rate elements, or are not reassigned pursuant to separations reform, be recovered, at least in part, through increased end user common line charges. U S West also suggests that we establish a separate fund similar to the universal service fund, with IXCs contributing to the fund on a flat-rate basis equal to their percentage share of switched access MOU. U S West further recommends revising the price cap rules to establish a formula for a flat-rated TIC.[383] SWBT proposes establishing a "Public Policy" rate element containing the costs associated with providing transport facilities and services to low-volume, rural areas and a significant portion of tandem switching costs.[384]

113. In a similar vein, GTE proposes permitting incumbent LECs to recover any remaining TIC costs through a flat-rate "regulatory policy cost recovery" charge.[385] Under GTE's proposal, incumbent LECs would submit separations-based cost studies to the FCC showing the amount of marketing expense erroneously assigned to the interstate jurisdiction under existing FCC rules and residual TIC revenue requirement remaining after reallocation of specific costs to other rate elements.[386] Under GTE's plan, incumbent LECs would make corresponding adjustments to their newly-created "Network Services basket" PCI to reflect removal of marketing expenses and reassignment of TIC costs to other access elements. GTE's regulatory policy cost charge would be assessed on a bulk-billed basis to all telecommunication carriers that purchase interstate switched access, transport and network facilities used to provide interstate services from incumbent LECs. GTE asserts that the method is fair because it charges all carriers using incumbent LEC networks.[387] GTE submits that the regulatory policy charge should be capped at its initial value for one year, although an incumbent LEC would be permitted to charge less than the initial value. GTE argues that the regulatory policy charge should not be subject to price cap regulation because it is an explicit subsidy recovery and not representative of specific services provided to customers. Annual adjustments to the regulatory policy charge would be limited to the changes in costs allocated

[382] BA/NYNEX Reply at 39-40.

[383] U S West Comments at 71-73.

[384] SWBT Reply at 11.

[385] GTE Comments at 39, 41-44.

[386] GTE Comments at 42.

[387] GTE Comments at 43.

to the interstate jurisdiction that are being recovered by this charge.[388]

114. Teleport states that once the review of incumbent LEC switched access costs has been completed, the Commission will be able to determine what costs, if any, should remain in the TIC, and how any unrecovered costs can be recovered. Teleport recommends that any residual amounts be recovered through a uniform surcharge on all related rate elements subject to competition, which will ensure that the charges are cost based.[389] Subsequently, Teleport clarified that it believed that the TIC should not be assessed on carriers that do not use incumbent LEC transport facilities.[390] Sprint and Time Warner also recommend that the Commission preclude incumbent LECs from assessing the TIC on traffic that is carried to or from incumbent LEC end offices on the facilities of a competitor because that would require CAPs to pay for the costs of their competitors' services.[391]

115. Time Warner argues that the Commission should reject incumbent LEC proposals to establish a separate recovery mechanism, such as bulk billing, to preserve incumbent LEC revenue requirement recovery because they would reinstate the largely discredited rate base, rate-of-return regulatory structure and its associated harmful incentives.[392]

116. Several parties commented on pricing flexibility as a vehicle to address costs in the TIC. Aliant argues that after incumbent LECs shift TIC amounts into the appropriate existing or new rate elements, LECs should have the flexibility to shift any remaining TIC amounts into Transport and Tandem Switched zones, noting that this would allow the market to determine if these costs are recoverable.[393] Cable & Wireless states that TIC deaveraging would be acceptable once the charge is purged of inappropriate costs, provided that deaveraging is based on differences in the remaining costs. Cable & Wireless argues that incumbent LECs should not be allowed to recover revenue via the TIC in order to ensure revenue-neutrality in a regulatory environment intended to be devoid of implicit subsidies.[394]

---

[388] GTE Comments at 44.

[389] Teleport Comments at 32-33.

[390] Letter from Judith Herrman, Manager, Federal Regulatory Affairs, Teleport, to Richard Lerner, Competitive Pricing Division, April 11, 1997.

[391] Sprint Comments at 30; Time Warner Comments at 15; ACC Long Distance Comments at 12.

[392] Time Warner Reply at 22.

[393] Aliant Comments at 3.

[394] Cable & Wireless Comments at 22.

If deaveraging is permitted, Cable & Wireless contends that the Commission should ensure that all incumbent LECs deaverage in a consistent manner using geographic zones demarcated by actual cost differences, e.g., cost differences for an efficient local exchange provider using forward-looking technology. Cable & Wireless notes that every study area may not include all zone types, and there may be a need for more than three zones to minimize residual averaging within zones.[395] To the extent that direct-trunked transport rates understate the costs of transport in less-dense areas because they are based on special access rates in high-density areas, Sprint states that the Commission could allow density-based deaveraging of direct-trunked transport rates without the constraints that presently exist.[396]

117. TCA argues that incumbent LECs should be given greater flexibility to add rate elements or change rates as portions of the TIC are more clearly identified.[397] On the other hand, TRA opposes giving the incumbent LECs any significant flexibility as part of any associated transition.[398]

3. Approaches that Eliminate or Phase Out the TIC

118. Several parties contend that the TIC should be eliminated totally, or that any TIC amounts remaining after making any reallocations warranted by the record should be eliminated. MCI contends that there is no reason for the TIC once access cost elements are set to recover economic cost.[399] MCI argues that the TIC is an uneconomic, unnecessary, make-whole charge that should be eliminated. Moreover, MCI alleges that there is no basis for reallocating some of the TIC amount and renaming the rest the "public policy" rate element, which will force new entrants to pay an indefensible subsidy to their competitors.[400] MCI argues that Part 36 allocates incumbent LEC expenditures, not costs. MCI suggests that it is likely incumbent LEC spending is not at the economically efficient level, given the current absence of effective competition and the price cap plan that does not effectively pass through to ratepayers changes in incumbent LEC costs. MCI states that the Hatfield model indicates that the incumbent LECs' spending is approximately $10 billion above their true

[395] Cable & Wireless Comments at 22-23.

[396] Sprint Comments at 29.

[397] TCA Comments at 4.

[398] TRA Comments at 36.

[399] MCI Comments at 87.

[400] MCI Reply at 29.

costs.[401] Furthermore, MCI contends that the Hatfield model shows that incumbent LECs are not charging less than cost to provide local service.[402]

119. AT&T recommends eliminating the TIC immediately, suggesting that phasing the TIC out over some period might be inconsistent with the court's mandate in *CompTel v. FCC*. AT&T also asserts that the 1996 Act requires access to be priced at TELRIC levels, and contends that anything other than an immediate elimination of the TIC would violate that requirement.[403] AT&T also argues that the TIC should be eliminated immediately because: (1) the current per-minute TIC raises long distance rates above economic levels and restricts long distance usage, to the detriment of consumers ;[404] (2) the 1996 Act requires the Commission to remove implicit subsidies from access, and to price access at TELRIC;[405] (3) the TIC is anticompetitive and inconsistent with the Act's competitive goals because (a) it guarantees incumbent LECs recovery of transport "costs," even when their networks are not used;[406] and (b) it distorts competition by allowing incumbent LECs to price transport facilities below cost and thus below competitors' prices; and (4) the Court of Appeals has admonished the Commission to move expeditiously to a cost-based alternative or provide a reasoned explanation of why a departure from cost-based ratemaking is necessary, and no such justification exists here.[407]

120. CompTel asserts that the TIC should immediately be set to zero because by definition, it does not include any costs that will not be recovered by TSLRIC-based rates for other access elements.[408] Similarly, LCI argues that access charges should be priced using TELRIC method, and that the TIC should be eliminated as a non cost-based residual revenue stream that is at odds with the movement to cost-based pricing.[409] NCTA also argues that the

[401] MCI Reply at 27.

[402] MCI Reply at 27-28.

[403] AT&T Comments at 57-59.

[404] *Accord* WorldCom Comments at 65.

[405] *Accord* MCI Comments at 86; LCI Comments at 28.

[406] *Accord* Sprint Comments at 29-30; Teleport Comments at 14 n.8.

[407] AT&T Reply at 30-31.

[408] CompTel Reply at 2.

[409] LCI Comments at 28.

TIC should be eliminated immediately.[410] Telco Communications Group advocates reassigning the easily identifiable costs to facility-based elements and phasing out the balance of the TIC. The TIC allows the incumbent LECs to price access below cost and recover the shortfall, regardless of whether the incumbent LEC provides transport facilities to the carrier paying the TIC or not. As a result, Telco Communications Group says a collocated transport provider must meet or beat the incumbent LEC prices and pay the TIC as well.[411] TRA contends that costs in excess of forward-looking economic costs should be eliminated.[412]

121. ACC Long Distance contends that the TIC should be eliminated over a well-defined period of no more than three years.[413] Excel favors reassigning readily identifiable and quantifiable costs and prescriptively phasing out the remainder of the TIC over no more than three years.[414]

122. Ad Hoc supports the Commission's proposal to identify and reallocate costs in the TIC to the extent possible, and to either permit incumbent LECs to write off the remaining TIC costs, or to require incumbent LECs to treat those costs as they treat other residual costs.[415] LCI argues that incumbent LECs should not be permitted to assess the TIC on terminating traffic because it is not cost-based since there are no TELRIC-based costs to recover.[416] ITC asserts that the TIC should be viewed as a support mechanism and eliminated as part of the USF proceeding.[417]

123. The California Cable Television Association argues that any transport costs recovered by the TIC should be recovered through the transport element with the non-cost subsidy portion prescriptively phased.[418] Time Warner argues that incumbent LECs should be given a limited opportunity to recover costs in the TIC that are unassignable to other

[410] NCTA Comments at 3, 27.

[411] Telco Communications Group Comments at 5.

[412] TRA Comments at 36.

[413] ACC Long Distance Comments at 12.

[414] Excel Comments at 13-14.

[415] Ad Hoc Comments at 27-29.

[416] LCI Comments at 20.

[417] ITC Comments at 4.

[418] California Cable Television Association Comments at 12.

elements, such as amortizing them over a five-year period through proportionate allocation to interstate switched access rate elements.[419] TCI argues that the Commission should base all rates for transport facilities on forward-looking costs and phase out the recovery of other TIC cost, which approach, according to TCI, would be most consistent with the Court's remand. If the Commission wishes to allow the incumbent LECs continued recovery of any portion of legacy costs, it should do so through a PIC-based rate element, which would be phased out over time by transferring these costs to the SLC.[420]

124. The Oregon Commission states that any remaining costs should be phased out.[421] The Alabama Commission generally supports a solution in which costs would be reassigned to the transport facility elements to correct identifiable misallocations. The remaining revenue shortfall should be shifted to a separate fund or account, recovered on a competitively neutral basis, and phased out over a reasonable period of time. The Alabama Commission states that the TIC is an implicit subsidy that must be eliminated under the 1996 Act.[422]

125. The Texas Public Utility Counsel supports reassigning to transport facility rate elements those portions of the TIC that can be identified, including the TELRIC of the element plus a reasonable allocation of forward looking common costs, and shifting the remaining revenue shortfall to a specially identified account to be recovered on a competitively neutral basis and phased out over time. Increased levels of universal service support should be used to offset the amount of the TIC that is earmarked for phase-out.[423] The Texas Public Utility Counsel argues that the Commission should eliminate unnecessary economic cost recovery.[424] To the extent that there are uneconomic costs embedded in the TIC, AARP, *et al.* argues that they should be eliminated.[425] AARP, *et al.* states that using reductions in the rate of return to reduce the TIC is reasonable.[426]

126. USTA and most incumbent LECs assert that the TIC should not be phased out, contending instead that any costs remaining in the TIC after reallocation should be bulk-billed

[419] Time Warner Comments at 14.

[420] TCI Comments at 20.

[421] Ohio Commission Comments at 5-6.

[422] Alabama Commission Comments at 10-11.

[423] Texas Public Utility Counsel Comments at 21.

[424] Texas Public Utility Counsel Comments at 16.

[425] AARP, *et al.*, Comments at 17. *See also* State Consumer Advocates Comments at 36.

[426] AARP, *et al.*, Comments at 17.

to the IXCs based on interstate revenues or minutes until reform of the separations process is completed. These parties argue that all incumbent LECs are entitled to full and complete recovery of the TIC amount because the TIC represents actual, real costs that have been assigned to the interstate jurisdiction by the Commission's rules.[427] Puerto Rico Tel. asserts that the Commission is under no obligation to phase out the TIC based on the CompTel remand, and in fact, cannot ignore the real costs underlying the TIC in the guise of access charge reform.[428]

127. Minnesota Independent Coalition argues that there is no basis for assuming that certain investment costs included in the TIC should be removed because of imprudence or because such investments are no longer used or useful. Minnesota Independent Coalition contends that this issue cannot be determined on an industry-wide basis using assumptions that may be wholly inaccurate in the case of individual LECs, but must be determined on a company-by-company basis.[429] Several incumbent LECs contend that failure to allow recovery would constitute a breach of the regulatory contract, a denial of fundamental due process, and a Fifth Amendment taking.[430]

128. Ameritech asserts that a phase out of the TIC should only be mandated: (1) over a sufficiently long period of time (*e.g.*, five years) to permit incumbent LECs and state commissions to manage the revenue loss; (2) if the Commission adopts the market-based approach to access reform, which would give the incumbent LECs sufficient pricing flexibility to manage the revenue loss; and (3) the Commission permits price cap LECs to target mandatory price cap reductions to the TIC during the phase-out period. In addition, Ameritech says states should conduct proceedings to permit incumbent LECs to recover the intrastate portions of the loop and line port costs from end user rates or state universal service fund subsidies, because these facilities currently are partially subsidized from the TIC.[431] The Illinois Commission proposes that to the extent that it is not possible to reallocate the entire TIC to appropriate rate elements, rate reductions required by the price cap mechanism should

---

[427] *See, e.g.*, USTA Reply at 36-37; BellSouth Reply at 13-14; U S West Comments at 63-64; SWBT Reply at 12; Aliant Comments at 2; SNET Reply at 27-28; ALLTEL Reply at 8; Puerto Rico Tel. Reply at 11-12; Rural Tel. Coalition Reply at 13-15; TCA Comments at 4; TDS Comments at 23; Western Alliance Comments at 22.

[428] Puerto Rico Tel. Comments at 16-17.

[429] Minnesota Independent Coalition Comments at 17.

[430] Roseville Tel. Comments at 10; Minnesota Independent Coalition Comments at 17.

[431] Ameritech Reply at 32-33.

be focused on the TIC until it is phased out.[432]

129. Several incumbent LECs concur with Ameritech on targeting price cap reductions to the TIC until the TIC is phased out, although disagreeing with Ameritech's idea to phase out the TIC over a fixed number of years. For example, PacTel suggests that, if the Commission continues to use a productivity factor, it could include a new "productivity offset" where the productivity factor could be targeted to the remaining TIC, gradually eliminating it over a number of years.[433] Sprint also proposes to target all of the price cap productivity adjustment at the TIC until it is eliminated. Sprint states that a price cap productivity adjustment would eliminate the TIC in five years or less for all but three price cap LECs, without having to explore in detail the cost components of the TIC, or possibly revise Parts 36 and 69.[434] Sprint indicates that the TIC would be eliminated within 7 years for the other 3 price cap LECs. Sprint states that it may be possible to phase out the TIC immediately if increases in explicit universal service subsidies to price cap LECs, with offsetting reductions in the interstate access charges, are large enough.[435] During the phase out, Sprint contends that the TIC should continue to be recovered on a per-minute basis, instead of using bulk-billing mechanisms based on presubscribed lines or retail IXC revenues. Recovery in bulk would insulate the incumbent LECs from competition because they would recover the TIC even if LEC competitors provided the access.[436]

130. ALTS argues that the Commission should not adopt Sprint's proposal to phase out the TIC by applying the productivity factor against it only. ALTS argues that such targeting would undercut the rationale for the "just and reasonable" status of all price-cap rates, which is the widespread application of the X-factor. According to ALTS, there are no sound policy reasons for Sprint's approach. Instead, the TIC should be curing identifiable cost misallocations and reducing the remainder via competition in the tandem market.[437] ALTS states that a long-term phase down of any remaining costs in the TIC is a fallback option.[438]

---

[432] Illinois Commission Comments at 13.

[433] PacTel Comments at 72; *See also* BA/NYNEX Comments at 38.

[434] Sprint Comments at 29, 51, Exhibit 8; Sprint Reply at 17-18.

[435] Sprint Reply at 17.

[436] Sprint Reply at 19.

[437] ALTS Reply at 24.

[438] ALTS Comments at 26.

E. SS7 Signalling

131. A number of commenters support adopting the Ameritech rate structure for general application to all price cap LECs.[439] TCI argues that an unbundled SS7 rate structure would allow customers and market entrants to obtain access efficiently by purchasing only the SS7 network functions they require. TCI further supports flat-rated charges for signal links and STP port termination.[440] Although Time Warner supports adoption of the Ameritech rate structure, it cautions against the creation of overly detailed rules, suggesting that detailed rules for SS7 services are unnecessary.[441] AT&T supports adoption of the Ameritech rate structure but acknowledges that some LECs lack facilities to measure SS7 usage which justifies delaying implementation of the unbundled rate structure.[442] MCI supports the concept of an unbundled SS7 rate structure, but argues that rates for particular sub-elements could be more cost-based than the Ameritech rate structure.[443] Illuminet also supports general use of the Ameritech rate structure, but urges the Commission to impose strict tariff requirements to ensure that rates are just and reasonable. As for specific elements, Illuminet, like TCI, favors flat-rated charges for signal links and STP port termination because they reflect specific SS7 functions dedicated to specific customers.[444]

132. Generally, incumbent LECs oppose mandating the implementation of the Ameritech SS7 rate structure. BellSouth and GTE oppose a specific rate structure for signalling because it would require the acquisition and deployment of equipment to measure usage of SS7 services.[445] In addition, BellSouth argues that the Ameritech rate structure does not provide adequate flexibility to address the use of future signalling services, such as advanced intelligent networks (AIN).[446] Similarly, Bell Atlantic and NYNEX oppose mandating the Ameritech SS7 rate structure because they, too, lack the ability to track costs associated with the use of disaggregated SS7 services.[447] If the Commission imposes an

---

[439] TCI Comments at 22-23; Time Warner Comments at 16-17; Illuminet Comments at 2-4.

[440] TCI Comments at 22.

[441] Time Warner Comments at 17.

[442] AT&T Reply at 33-34.

[443] MCI Comments at 87.

[444] Illuminet Comments at 2-4.

[445] BellSouth Comments at 81; GTE Comments at 53.

[446] BellSouth Comments at 82.

[447] Bell Atlantic/NYNEX Comments at 40.

unbundled structure similar to Ameritech's, Bell Atlantic and NYNEX request that the Commission allow recovery of all direct costs incurred to enable billing for specific rate elements. They estimate this cost would range between $15 million and $40 million.[448] Other RBOCs echo similar concerns regarding equipment requirements to measure unbundled SS7 services.[449] Ameritech itself argues against a general requirement that its SS7 rate structure be implemented for all price cap LECs. It contends that its rate structure may not be appropriate on an industry-wide basis and that use of the Ameritech SS7 rate structure should be permissive.[450]

133. Other commenters caution against mandating the Ameritech rate structure. CompTel suggests that Ameritech's SS7 structure may be appropriate in the future, but should not be mandated now because carriers lacking necessary metering equipment would have to develop measuring capabilities that would place significant financial and operational burdens on smaller carriers.[451] Similarly, Worldcom argues that the high costs associated with measurement and billing facilities outweigh the benefits of adopting Ameritech's rate structure on an industry-wide basis.[452]

134. Generally, commenters choosing to discuss the ISUP/TCAP issue do not favor the imposition of separate charges for ISUP and TCAP messages. They expressed concern that the cost of implementing such an approach and monitoring message lengths with sufficient particularity would not justify the benefits to be derived from the proposed rate differentiation.[453] AT&T suggests rate differentiation between ISUP and TCAP messages should be permissive.[454]

135. With respect to the treatment of signalling rate elements in price cap baskets, both MCI and AT&T advocate placing STP port termination in the traffic-sensitive basket while leaving the signalling link in the trunking basket. These commenters argue that STP port termination is not subject to competitive provision which justifies placement in different

[448] *Id.* at 40 n.95. *See also* USTA Comments at 66 and Reply at 37. Sprint estimates that the cost of metering equipment would run between $15 million and $20 million. Sprint Comments at 31.

[449] PacTel Comments at 73; SBC Comments at 15.

[450] Ameritech Comments at 23. *See also* US West Comments at 73-74.

[451] CompTel Comments at 31-32.

[452] Worldcom Reply at 39-41.

[453] MCI Comments at 89; Time Warner Comments at 17; CompTel Comments at 31-32.

[454] AT&T Comments at 61.

baskets.[455] AT&T contends that incumbent LECs have an incentive to respond to competitive pressures in their signal link business by raising the level of the STP port charge.[456] Ameritech, on the other hand, opposes shifting STP port charges to the traffic-sensitive basket, arguing that any concern that STP port charges would be used to offset price reductions for the signal link is unfounded. Increases in the STP port termination charge, Ameritech contends, would encourage its customers to find other means to interconnect with the incumbent LEC's network.[457]

F. Impact of New Technologies

136. Incumbent LECs oppose the adoption of specific or detailed rate structures for recovery of costs associated with new technologies. According to USTA, a mandated rate structure would create a disincentive for LECs to invest in the development of new technologies.[458] Ameritech cautions against the adoption of rate structures, arguing that fast changing technology will render detailed rate structures outdated.[459] BellSouth advocates general rate structure guidelines rather than specific rules because flexibility will promote greater customer service choices.[460] GTE also opposes new rate structures for advanced technologies because detailed regulation would impair the ability of incumbent LECs to respond to competition from competitive LECs that also deploy new technologies.[461]

137. Other commenters support the development of cost-causative rate structures for certain technologies. AT&T favors adoption of a rate structure for SONET, recommending that this technology be priced on a flat, distance-sensitive basis. AT&T also advocates the establishment of per-message charges to recover the costs of AIN databases.[462] ALTS agrees that cost-causative rate structures for SONET and AIN should be adopted because these technologies are sufficiently mature to permit identification of their costs.[463] Other

---

[455] MCI Comments at 87-88; AT&T Reply at 33-34.

[456] AT&T Reply at 33-34.

[457] Ameritech Comments at 24-25.

[458] USTA Reply at 37. *See also* PacTel Comments at 73.

[459] Ameritech Comments at 25.

[460] BellSouth Comments at 83.

[461] GTE Comments at 53.

[462] AT&T Comments at 62-63.

[463] ALTS Reply at 25.

commenters, however, oppose the adoption of rate structures for new technologies, arguing that the deployment of a new technology to provide access services should lower the costs of providing access and promote efficiency. These commenters argue that new technologies merely change the cost of providing a traditional service and do not justify the adoption of corresponding rate structures.[464]

IV. BASELINE RATE LEVELS

A. Primary Reliance on a Market-Based Approach With Adoption of Several Initial Prescriptive Measures

138. Nearly all commenters agree that competition in markets for local exchange services, including exchange access services, is likely to produce lower interstate access prices. There is sharp disagreement, however, about the extent to which competition has developed, or will soon develop, to the point where it can be relied on to produce lower access charges. It is this disagreement that is largely responsible for parties' differing positions concerning the advisability of adopting either a market-based or a prescriptive approach to access charge reform.

139. *Support for a Market-Based Approach.* DOJ and most LECs support a market-based approach to reform of access charge rate levels. DOJ comments that a market-based approach will permit a more gradual transition to cost-based access charges, which will permit a more orderly and appropriate treatment of issues concerning universal service support and jurisdictional separations.[465] DOJ also recommends that the Commission adopt a prescriptive backdrop to its market-based reform. Incumbent LECs argue that market forces are more reliable and more precise than regulation for aligning rates with costs.[466] They also argue that the efficient operation of competitive markets requires that incumbent LECs be given the pricing flexibility embodied by the market-based approach sooner rather than later.

140. Most incumbent LECs combine their support for a market-based approach with opposition to a prescriptive approach to reforming access charge rate levels. Several incumbent LECs and other parties contend that the prescriptive approach is less likely than the

[464] Spectranet Comments at 6; TCI Comments at 24; Illinois Commerce Commission Comments at 14.

[465] DOJ Ex Parte at 17-21.

[466] Alaska Tel. Assoc. Comments at 2-5; Aliant Comments at 3-4; Ameritech Reply at 3-8; BA/NYNEX Comments at 2-4; BellSouth Comments at 11, 14-16, 28-29; Cincinnati Bell Comments at 12-13; GTE Comments at 19-21; Independent Telephone and Telecommunications Alliance Comments at 5; PacTel Comments at 11-17; SNET Comments at 2-3, 6-7; TDS Comments at 28-32; USTA Comments at 32-34; and U S West Comments at 20-29.

market-based approach to result in economically efficient rates.[467] Some incumbent LECs also argue that a static prescriptive approach would not reflect fluctuations in supply and demand as a competitive market would.[468] Some commenters maintain that the prescriptive approach would result in inefficient rates, and thus skew potential competitors' entry decisions.[469] Cincinnati Bell opposes the prescriptive approach because it could result in more rapid rate reductions than would occur in a competitive market.[470] Citizens Utilities argues that the prescriptive approach would discourage use of unbundled network elements and retard the development of competition.[471]

141. Several commenters claim that the prescriptive approach is essentially an abandonment of price cap regulation, because it would punish incumbent LECs for efficiency gains made under the price cap regime.[472] Some incumbent LECs argue that the Commission determined that the initial price cap rates were reasonable, and that there is no basis to reverse that finding now.[473] BA/NYNEX argues that the prescriptive approach would be substantially similar to rate-of-return regulation, with recurring rate cases needed to recalculate forward-looking costs in light of further technological improvements. BA/NYNEX argues further that this would vitiate price cap regulation and create a disincentive for future investment.[474] Some incumbent LECs assert that the prescriptive approach unreasonably discourages

---

[467] *See, e.g.*, Ameritech Comments at 48-49, Attachment B at 4; BA/NYNEX Comments at 2; BellSouth Comments at 41; Illinois Commission Comments at 23-25; CSE Comments at 4-5; Cincinnati Bell Comments at 13; GTE Comments at 74; SNET Comments at 23; American Communications Reply at 2-6.

[468] BellSouth Comments at 14-15; USTA Comments, Attachment 1 at 15; BellSouth Reply at 28-30; Ameritech Reply at 7, 19 and Attachment 1 at 16; USTA Reply, Attachment 1 at 10-11, Attachment 2 at 46; Attachment 3 at 7.

[469] Ameritech Comments at 49; PacTel Comments at 5; ALTS Comments at 21-22; Ohio Commission Reply at 6-7; USTA Reply at 10-11; U S West Reply at 7-10. U S West speculates that AT&T and MCI are seeking to limit entry into the local exchange market, in order to delay BOC entry into the long-distance market. U S West Reply at 8-9.

[470] Cincinnati Bell Comments at 13.

[471] Citizens Utilities Comments at 15.

[472] Ameritech Comments, Attachment B at 22-23; BA/NYNEX Comments, Attachment 1 at 4; USTA Comments at 12; PacTel Comments at 30; U S West Comments at 45-46; BA/NYNEX Reply, Attachment 1 at 2, 5-6; GTE Reply at 41. *See also* BellSouth Comments, Attachment 2 at 25 (observing generally that reducing profits too much might adversely affect efficiency incentives).

[473] GTE Reply at 40-41; PacTel Reply at 12; SWBT Reply at 21, *citing LEC Price Cap Order*, 5 FCC Rcd at 6814-17.

[474] BA/NYNEX Comments, Attachment 1 at 7. *See also* BellSouth Reply at 36.

incumbent LECs' investment in their networks.[475] AT&T replies that, because price cap LECs would still be able to increase their profits by increasing their productivity growth, price cap regulation and its incentives for investment would remain in effect.[476] Competition Policy Institute argues that the opening of exchange access markets to competition means that lower rates of return are unlikely to stifle innovation, because competitive pressure will spur innovation.[477]

142. According to BellSouth, if access rates do not comport with market-based levels, it is because of regulatory policies rather than incumbent LEC inefficiency. BellSouth opposes the prescriptive approach because it does not address those regulatory policies.[478] Similarly, several parties assert that we cannot adopt a prescriptive approach unless we establish a joint board to increase the allocation of costs to the intrastate jurisdiction.[479]

143. Local exchange carriers generally argue that they already face substantial competition, particularly for exchange access services.[480] In addition, they argue that competition will develop first, and most rapidly, for the very customers that generate the majority of exchange access minutes.[481] In particular, they argue that barriers to entry are quite low in local markets, particularly for the provision of exchange access services, now that

[475] Ameritech Comments at 49; BA/NYNEX Comments, Attachment 1 at 3; BellSouth Comments at 41-42; Ameritech Reply, Attachment A at 11; BA/NYNEX Reply at 15-16; PacTel Reply, Testimony of Bruce Egan at 24-25 (Egan Aff.); USTA Reply at 7-8, 11-12, and Attachment 1 at 1-2; U S West Reply at 7; USTA Reply, Attachment 1 at 9-10. *See also* American Association for Adult and Continuing Education, *et al.* Reply at 9-11.

[476] AT&T Reply at 18.

[477] Competition Policy Institute Comments at 24-25.

[478] BellSouth Comments at 15. *See also* USTA Comments, Attachment 2 at 12-19; U S West Reply at 5-6; USTA Reply, Attachment 1 at 3-4.

[479] BA/NYNEX Comments at 21-23 and Ex. 2; PacTel Comments at 31-32; Illinois Commission Comments at 25-26; Harris, Skrivan & Associates Comments at 3; Oregon Commission Comments at 2-3; TDS Comments at 28; Evans, *et al.* Comments at 10-11; API Reply at 17-18; Ohio Commission Reply at 2-3; Time Warner Reply at 22-23. The Tennessee Commission advises against a "rush to judgment" in this proceeding before a joint board can review separations changes. Tennessee Commission Comments at 2-3.

[480] *E.g.*, Ameritech Comments at 33-35; BellSouth Reply at 20-24; GTE Comments at 10-17; PacTel Comments at 11-15; SWBT Comments at 33-34; SNET Comments at 11-15; USTA Reply at 30; and U S West Comments at 22-23.

[481] *E.g.*, BA/NYNEX Reply at 22-26; Cincinnati Bell Comments at 15-20; and U S West Reply at 36-38.

unbundled network elements are available to competitors at cost-based rates.[482] BellSouth states that, regardless of whether the market today is sufficient to restrain access prices, we should still incorporate market principles into the regulatory regime.[483]

144. *Opposition to a Market-Based Approach.* Several parties argue that market forces will not be adequate to drive access rates to forward-looking cost in the near future.[484] AT&T and MCI argue that the provisions of the 1996 Act require that explicit and implicit cross-subsidies have to be removed from interstate access charges, and that this must be done more quickly than can occur under a market-based approach to access charge reform.[485] Intl. Comm. Ass'n also argues that the local exchange and exchange access markets are not competitive, and that we cannot rely on unbundled network elements to drive rates down as long as some of our Part 51 rules are stayed.[486] The Missouri Commission and AT&T argue that competition will be slow to develop, particularly with respect to terminating access.[487] Ad Hoc favors a prescriptive approach, because it ensures that prices will be reduced to forward-looking economic costs regardless of the presence or absence of competition.[488] TDS asserts that both the prescriptive and the market-based approach would increase Commission control over incumbent LEC pricing decisions, and therefore neither are likely to result in

---

[482] BA/NYNEX Comments at 13; BellSouth Commenst at 23-27; SNET Reply at 2-3, 6-7; and USTA Comments at 32-34.

[483] BellSouth Reply at 27-28.

[484] ACC Long Distance Comments at 9; AT&T Comments at 20-21; ACTA Comments at 20; America On-Line Comments at 11-12; Competition Policy Institute Comments at 9-11; SDN Users Association Comments at 1-2; Internet Access Coalition Comments at 8-9; NCTA Comments at 21; LCI Comments at 8-17; CompTel Comments at 13-15; Excel Comments at 7-9; Florida Commission Comments at 7; California Cable Television Association Comments at 10-11; Tennessee Commission Comments at 4; Texas Public Utility Counsel Comments at 4-5; TRA Comments at 6-18; Washington Commission Comments at 7-8; API Reply at 2-4, 12-15; AT&T Reply at 4-8; GCI Reply at 3-4; IXC Long Distance, Inc. Reply at 3-4; Ohio Consumers Counsel Reply at 7-8; Sprint Reply at 20-21; TCI Reply at 20-22; Telco Communications Group Reply at 3. *See also* Frontier Comments at 10-11; GSA/DOD Comments at 19; State Consumer Advocates Comments at 53; Texas Commission Comments at 23-24 (supporting prescriptive approach in short term, followed by a transition to a market-based approach). TCI recommends a prescriptive approach for incumbent LECs and forbearance for competitive LECs, and describes this as a "combination" approach. TCI Comments at 25-27.

[485] AT&T Comments at 63-71; MCI Comments at 42-43.

[486] Intl. Comm. Ass'n Comments at 2-4.

[487] Missouri Commission Comments at 4-5; AT&T Reply at 6-7.

[488] Ad Hoc Comments at 37.

efficient pricing.[489]

145. Long-distance carriers, which are the customers of switched access services, argue that competition in local markets largely does not exist today. In addition, they argue that entry into local markets, which have historically been characterized by monopoly provision of services, will take much longer than will LEC entry into long-distance markets, where many customers are accustomed to switching carriers and the operational support systems and procedures for switching carriers are well developed. AARP *et al.* notes that BellSouth and U S West have advocated a prescriptive approach based on TELRIC in interconnection proceedings in other countries, because competition in those countries is not sufficient to drive rates to cost.[490] According to AARP *et al.*, BellSouth has also argued in foreign proceedings that the incumbent has an inherent advantage over new entrants because of factors such as name recognition and customer inertia.[491]

146. Some IXCs and other parties argue that incumbent LECs will fight competitive entry as long as they can.[492] According to LCI and MCI, incumbent LECs are filling interconnection orders slowly and that this is preventing the development of competition.[493] LCI provides a list of service ordering and provisioning procedures that it claims are necessary for local exchange competition to develop, and considers these procedures to be a prerequisite for any market-based reforms.[494] LCI maintains that the incumbent LECs' control of the local networks gives them a competitive advantage, and that the policies adopted in the 1996 Act and the *Local Competition Order* will not lead to competition unless the Commission enforces its rules and properly manages the transition to competition.[495] LCI doubts that resale will lead to competition, because setting wholesale prices at retail minus

---

[489] TDS Comments at 29-31.

[490] AARP *et al.* Comments at 7-17.

[491] AARP *et al.* Reply at 21-22.

[492] ACC Long Distance Comments at 4-9; AT&T Comments, Attachment A at 20-21; IXC Long Distance, Inc. Comments at 3-4; AARP *et al.* Reply at 7-8; TCI Reply at 22-23. In its reply, IXC Long Distance, Inc. alleges several specific instances in which SWBT and GTE have engaged in anticompetitive conduct to delay interconnection. IXC Long Distance, Inc. Reply at 4-9. GTE denies that any litigation it has initiated was a ploy to delay interconnection. GTE Reply at 35. ACC Long Distance claims it has experienced "repeated delays" in obtaining physical collocation. ACC Long Distance Reply at 5-6.

[493] LCI Comments at 15; MCI Reply at 32-33.

[494] LCI Reply at 3 and Attachment. *See also* AT&T Reply at 14-15; CompTel Reply at 4-5; Sprint Reply at 19-20 and Attachment; WorldCom Reply at 19.

[495] LCI Comments at 8-12.

avoided costs does not permit a new entrant to be profitable enough to construct its own facilities, and because such wholesale pricing is above forward-looking economic cost.[496] MCI maintains that incumbent LECs are using non-recurring charges as a means of discouraging competitive entry.[497] AT&T also criticizes incumbent LECs for failing to provide dialing parity and adequate access to operations support systems.[498] According to LCI, the incumbent LECs' local switches do not permit all interconnectors equal access.[499] AT&T asserts that the prohibition against interconnectors using unbundled network elements for access unless they have also won the local customer creates an unreasonable barrier to entry and will ultimately limit the development of local competition.[500] GTE replies that it provides nondiscriminatory access to its operational support systems.[501]

147. AT&T cites to *Farmers Union Central Exchange, Inc. v. FERC*[502] for the proposition that "[r]eliance on competitive forces to constrain exchange access rates, particularly in the presence of strong indications that market forces will not produce the intended results, would be arbitrary and capricious and contravene the Commission's statutory duty to ensure just, reasonable, and nondiscriminatory rates."[503] PacTel challenges the relevance of *Farmers Union*, arguing that the mandate Congress gave FERC was regulatory, whereas Congress in the 1996 Act stated that competition rather than regulation should be used to set rates for telecommunications services.[504]

148. *Support for a Combination of Market-Based and Prescriptive Measures.* ICG recommends four years of phased-in access charge reductions, while competitive LECs construct facilities-based networks. After this period, ICG suggests that some form of a

---

[496] LCI Comments at 12-13. *See also* ALTS Reply at 11-12 (resale followed facilities-based competition in interexchange market, so resale is less likely than facilities-based competition to provide competitive pressure in access market).

[497] MCI Reply at 33-34.

[498] AT&T Reply at 10-12.

[499] LCI Comments at 13. *See also* AT&T Reply at 10.

[500] AT&T Reply at 8-9.

[501] GTE Reply at 35.

[502] 734 F.2d 1486, 1508 (D.C. Cir.) (*Farmers Union*), *cert. denied*, *Williams Pipe Line Co. v. Farmers Union Central Exchange, Inc.*, 469 U.S. 1034 (1984).

[503] AT&T Comments at 48.

[504] PacTel Reply at 14-16.

market-based approach would be reasonable.[505] A number of parties, including several state commissions, advocate similar approaches.[506] The District of Columbia Commission recommends that we retain authority to re-impose regulatory control after we permit some pricing flexibility, in case the competitive conditions that warranted granting the pricing flexibility change.[507]

149. WorldCom suggests using a combination of "carrots" and "sticks" to induce the incumbent LECs to facilitate local competition. WorldCom's "carrot" to induce such compliance would be the promise of future pricing flexibility, and the "stick" would be the threat of prescriptive rate changes.[508] Specifically, WorldCom would give incumbent LECs until January 1, 1999, to implement unbundled network element requirements, and then impose prescriptive requirements.[509] USTA argues that the prescriptive approach should be used, if at all, only if there is considerable evidence that current market forces are insufficient to reform the current access market.[510] On the other hand, BellSouth opposes using the prescriptive approach as a "backstop" to a market-based approach, because it does not believe the Commission can specify a set of circumstances that indicate a market failure.[511]

150. The California Commission supports a market-based approach in competitive areas, and a prescriptive approach in areas that are "not sufficiently competitive." The California Commission would define a competitive market as one where a serving wire center is providing unbundled elements to at least one competitor unaffiliated with the incumbent LEC, provided the incumbent meets the other proposed Phase 1 criteria.[512] AT&T maintains that the growth of competition resulting from the availability of unbundled network elements will be slower in rural areas, and so the market-based approach would be less effective in

---

[505] ICG Comments at 15-17.

[506] Ad Hoc Comments at 46; Competition Policy Institute Comments at 9-14; Frontier Comments at 10-11; NCTA Comments at 20-24; Alabama Commission at 11-13; District of Columbia Commission Comments at 1-3; Florida Commission Comments at 5; Texas Commission at 23-26; NARUC Comments at 10; MCI Reply at 2-5.

[507] District of Columbia Commission Comments at 3.

[508] WorldCom Comments at 72-73. *See also* Ameritech Comments, Attachment B at 22-23; American Communications Reply at 6-7, 15-16.

[509] WorldCom Comments at 89-91.

[510] USTA Comments, Attachment 1 at 15.

[511] BellSouth Comments at 16-17.

[512] California Commission Comments at 7-10.

rural areas than in urban areas.[513]

151. Competition Policy Institute recommends imposing prescriptive measures simultaneously with market-based regulatory reforms. In addition to increasing the X-Factor and reinitializing PCIs, Competition Policy Institute suggests that the Commission: (1) facilitate the provision of unbundled elements;[514] (2) adopt a time frame for a transition of access charges to economic cost; and (3) annually review the progress of access charges toward economic cost, with the possibility of imposing additional prescriptive rate reductions if required.[515] AT&T argues that since whatever benefits of permitting incumbent LECs additional pricing flexibility do not relate to the levels of access charges, if the Commission insists on permitting additional pricing flexibility, it could do so in conjunction with the prescriptive approach.[516]

152. *Price Squeeze Concerns.* Some IXCs and AARP *et al.* are concerned that BOCs might cross-subsidize long-distance service with access revenues when they are permitted to enter the long-distance market pursuant to section 271, or engage in a price squeeze, unless we adopt a prescriptive approach.[517]

153. A number of incumbent LECs deny that any prescriptive measures are needed to prevent price squeezes because it is almost impossible to engage in a price squeeze profitably.[518] Moreover, the Communications Act or Commission regulations adequately

[513] AT&T Comments at 47-48.

[514] Specifically, Competition Policy Institute recommends the following: (1) eliminating the application of access charges to unbundled network elements; (2) monitoring state pricing decisions regarding unbundled network elements for consistency with TELRIC pricing standards; (3) minimize logistical barriers to the provisioning of unbundled network elements; (4) requiring subloop unbundling; (5) establishing an expedited complaint process available to unbundled network element purchasers; (6) periodic performance audits or surveys of the RBOCs' provisions of unbundled network elements; and (7) additional deaveraging of unbundled network element prices. Competition Policy Institute Comments at 26.

[515] Competition Policy Institute Comments at 25-27. *See also* GSA/DOD Comments at 13-15, 20-25; GSA/DOD Reply at 13-17; *NTIA Letter* at 4.

[516] AT&T Comments at 21.

[517] ACC Long Distance Comments at 9; AT&T Comments at 13-17 and Attachment A at 12, 20; Telco Communications Group Comments at 2-4; MCI Comments at 10-11, 14, 41; and Attachment at 12-13; Excel Comments at 4-5; AARP *et al.* Comments at 9-10; LCI Reply at 3-4.

[518] Ameritech Comments at 48; ALTS Reply at 18-19; Ameritech Reply at 22-23; BA/NYNEX Reply at 13; GTE Reply at 36; PacTel Reply at 19; U S West Reply at 10; USTA Reply at 31-32, Attachment 1 at 18, Attachment 3 at 13.

protect against price squeezes.[519] BellSouth also claims that, as long as it sets prices below "general market levels
or the costs of a firm's competitors," it has not legally engaged in a price squeeze.[520] U S West argues that the relevant factor for determining whether a carrier has committed a price squeeze is not the price level, but the margin between price and cost.[521] Alternatively, ALTS asserts that incumbent LECs have sufficient funds to finance price squeezes regardless of whether we adopt a prescriptive approach to access reform.[522] USTA argues that AT&T presents a similar threat of cross-subsidization of local service with long-distance revenues.[523] USTA also alleges that AT&T is seeking to limit competitive entry into the long-distance market.[524] Ameritech asserts that prescribing access rates that are too low might place competitive LECs that rely on unbundled network elements in a price squeeze.[525]

154. *Cross-Subsidization Concerns*. MCI argues that price cap regulation by itself does not eliminate incumbent LEC incentives to engage in anticompetitive cross-subsidization that might occur under a market-based approach.[526] NCTA advocates a prescriptive approach to protect against incumbent LEC cross-subsidization of video or other new services.[527] Similarly, many commenters argue that excessive access charges enable incumbent LECs to cross-subsidize any present or future competitive service.[528] The Texas Commission asserts

---

[519] Ameritech Reply at 22; BellSouth Comments at 18, *citing* 47 U.S.C. §§ 272(e)(3), 201, 202, 272(d); ALTS Reply at 17-18, 21; BA/NYNEX Reply at 12-13 and Attachment 1 at 2; GTE Reply at 35-36; PacTel Reply at 20-21; SWBT Reply at 32-34; USTA Reply at 31 and Attachment 3 at 12; U S West Reply, Attachment A at 4-5.

[520] BellSouth Comments at 18, *citing Brooke Group v. Brown & Williamson*, 509 U.S. 209, 223 (1993). *See also* USTA Reply, Attachment 1 at 17.

[521] U S West Reply, Attachment A at 4, *citing United States v. Aluminum Company of America*, 148 F.2d 416 (2nd Cir. 1945).

[522] ALTS Reply at 17.

[523] USTA Reply, Attachment 1 at 15-16.

[524] USTA Reply, Attachment 1 at 18.

[525] Ameritech Reply at 22-23.

[526] MCI Comments, Attachment at 10-13.

[527] NCTA Comments at 9.

[528] AT&T Comments, Attachment A at 9; Ad Hoc Comments at 39-41; GSA/DOD Reply at 15; TCI Reply at 23-24. CompTel argues that the Section 254(k) prohibition against cross-subsidization requires the Commission to prescribe TSLRIC-based rates. CompTel Reply at 10.

that it would be difficult to craft accounting rules to prevent incumbent LECs from cross-subsidizing with respect to multiple services in multiple geographical areas.[529]

155. The Georgia Commission recommends that whatever approach we adopt enable the incumbent LEC to recover all its prudently incurred costs rather than trying to shift costs to the intrastate jurisdiction. The Georgia Commission asserts that our first priority should be to facilitate competitive entry, and that price level regulation should be limited to monopoly services, to ensure that monopoly service prices are not too high or used to cross-subsidize competitive services.[530]

156. *Relative Administrative Burdens of the Possible Approaches.* Some parties argue that determining the extent of competition for each relevant market under the market-based approach would be more burdensome than any of the requirements of the prescriptive approach.[531] Cable & Wireless argues that the litigation surrounding the Phase 1 and Phase 2 determinations, the different negotiated agreements that will be adopted in each state, and the results of the court's review of the *Local Competition Order*, will result in a "patchwork" of different regulatory requirements, which would increase uncertainty in the market.[532]

157. A few parties maintain that the prescriptive approach would be unreasonably burdensome.[533] Teleport argues that a prescriptive approach might require annual reviews to verify that access rates were in fact moving towards costs.[534] ACC Long Distance denies that a prescriptive approach would be burdensome because it maintains that the Commission has substantial experience with such regulation.[535] A number of commenters assert that the prescriptive approach would increase regulatory control over the market, and therefore be

[529] Texas Commission Comments at 25-26.

[530] Georgia Commission Reply at 5-7.

[531] Excel Comments at 9-10; Florida Commission Comments at 4-5.

[532] Cable & Wireless Comments at 25-26. *See also* Intl. Comm. Ass'n Comments at 2-3; Kansas Commission Comments at 7-8.

[533] Illinois Commission Comments at 23-25; BellSouth Comments at 42; PacTel Comments at 28-29; ALTS Reply at 15-16; Ameritech Reply, Attachment A at 10; GTE Reply at 42; PacTel Reply at 13-14; USTA Reply at 12.

[534] Teleport Reply at 31-32.

[535] ACC Long Distance Reply at 6.

inconsistent with the 1996 Act.[536] AT&T replies that both the prescriptive and market-based approaches would retain price cap regulation initially, and so there is no reason to call one more regulatory than the other.[537]

158. *Prescriptive Measures Tailored for Insular or High-Cost Areas.* The Northern Marianna Islands support the prescriptive approach because it would enable the Commission to tailor access charge reforms to the unique circumstances faced in insular or high-cost areas such as the Northern Marianna Islands.[538] Alternatively, the Alaska Telephone Association argues that a market-based approach would better reflect local economic conditions, and so can be tailored to reflect the concerns of both large and small incumbent LECs.[539]

B. Prescriptive Approaches

1. Prescription of a New X-Factor

159. According to USTA, productivity estimates based on historical studies overstate the productivity potential of price-cap LECs under competition.[540] According to USTA, as incumbent LECs lose customers to competition, their output will decline, and as a result their measured productivity will decline. Therefore, USTA recommends basing the X-Factor on a five-year moving average of the TFP, so that reductions in productivity resulting from competition would be reflected in the X-Factor.[541] USTA claims that the TFP differential (TFP of LECs minus TFP for US economy as whole) is 2.7 percent, and will decrease by 0.4 percentage points each year if the Commission adopts USTA's recommendations for restructuring the CCL charge and the TIC.[542] Most incumbent LECs support USTA.[543]

---

[536] BellSouth Comments at 41; PacTel Comments at 5; USTA Comments at 11-12; TDS Comments at 29-31; SWBT Comments at 23-24; U S West Comments at 44-45; Aliant Comments at 3-4; Citizens Utilities Comments at 15. *See also* SNET Comments at 26.

[537] AT&T Reply at 18.

[538] Northern Marianna Islands Comments at 11-12.

[539] Alaska Telephone Association Comments at 2.

[540] USTA Comments at 19.

[541] USTA Comments at 20.

[542] USTA Comments at 21. *See also* USTA Reply at 41-42; US West Comments at 46-49; SWBT Reply at 37.

[543] BA/NYNEX Comments at 58-60; BellSouth Comments at 50 n.93; SNET Comments at 28-30; U S West Comments at 46-49; Aliant Reply at 3-4; BellSouth Reply at 41-42; SNET Reply at 24-25.

BA/NYNEX argues that productivity growth will decrease as a result of competition unleashed by the 1996 Act, and so basing the X-Factor on a five-year moving average TFP would likely overstate future achievable productivity.[544] Alternatively, BA/NYNEX argues that we could rely on a fixed TFP-based X-Factor for a short period of time, until Bell competition will enable us to deregulate incumbent LECs completely.[545] GTE and SNET contend that growth in competition and recovering more costs through flat rather than usage sensitive rates, will likely depress measured TFP growth.[546]

160. AT&T notes that it recommended at least 8.8 percent in its pleadings filed in response to the *Price Cap Fourth Further NPRM*.[547] Several commenters recommend setting the X-Factor at 9.9 percent, on the basis of the pleadings of the CARE Coalition filed in response to the *Price Cap Fourth Further NPRM* proceeding.[548] Ad Hoc also recommends increasing the X-Factor for the reasons it explained in its comments in the *Price Cap Fourth Further NPRM*.[549] MCI also supports increasing the X-Factor to 9.9 percent, but only for five years, after which MCI argues that the X-Factor should be based on TFP.[550] A number of price cap LECs maintain that the X-Factors recommended by AT&T and MCI greatly exceed their actual productivity growth under price cap regulation.[551] USTA has identified several purported computational and methodological errors in AT&T's, MCI's, and Ad Hoc's X-Factor proposals in its pleadings filed in response to the *Price Cap Fourth Further NPRM*.[552] Ad Hoc recommends making any fundamental changes to price cap regulation in the price cap proceeding, and focusing on access reform in this proceeding.[553] According to GTE, AT&T and Ad Hoc maintain that incumbent LECs' interstate productivity is greater than their

---

[544] BA/NYNEX Comments at 59. *See also* U S West Comments at 46

[545] BA/NYNEX Comments at 59; BA/NYNEX Reply at 29-30.

[546] GTE Comments at 57-58; SNET Reply at 25-26.

[547] AT&T Comments at 70. In its reply, AT&T increases its X-Factor recommendation to 9.0 percent, on the bases of updated data. AT&T Reply at 35 and Attachment G.

[548] API Comments at 27-28; ICA Comments at 4; WorldCom Comments at 91; API Reply at 18.

[549] Ad Hoc Comments at 70; Ad Hoc Reply at 7-14. Ad Hoc also replies that its *Price Cap Fourth Further NPRM* pleadings discredited USTA's X-Factor studies. Ad Hoc Reply at 9-14.

[550] MCI Comments at 25.

[551] BellSouth Comments at 50; BA/NYNEX Reply at 27-29; SWBT Reply at 37-39; Aliant Reply at 3.

[552] USTA Reply at 42-44. *See also* BA/NYNEX Reply at 30-31.

[553] Ad Hoc Reply at 7-8.

intrastate productivity, and included in their X-Factor recommendations an interstate TFP adjustment to account for this alleged difference in productivity. GTE further opposes any interstate TFP adjustment, because there incumbent LECs provide interstate and intrastate services using the same network, and so it would make no economic sense to assume that interstate productivity is greater than intrastate productivity.[554]

161. PacTel and Aliant propose setting the X-Factor equal to GDP-PI.[555] Sprint argues that the Commission should discontinue the use of the current productivity factor for all baskets except common line, once all access charges have been reduced to geographically deaveraged TELRIC levels.[556] AT&T anticipates that access reform would increase productivity growth, because reducing rates to cost-based levels would stimulate demand.[557]

2. Rejection of Certain Prescriptive Approaches

a. Rate Prescription

162. TRA and TCI recommend prescribing access rates because reinitializing PCIs would not guarantee that the LECs' rate structures would be reasonable.[558] Similarly, CompTel asserts that only a TSLRIC-based rate prescription can ensure that access rates are at cost-based levels.[559]

163. AT&T argues that a new rate prescription would not necessarily be burdensome, because four access rate elements account for most of the incumbent LECs' access revenue: the per-minute local switching charge, the per-minute tandem switching and common transport rate elements, and the dedicated transport elements. According to AT&T, it would be easy to reprice these four charges at forward-looking economic levels on the basis of existing TELRIC data.[560] Alternatively, AT&T argues that, even if a reinitialization were burdensome,

[554] GTE Reply at 27-28.

[555] PacTel Comments at 41-42; Aliant Comments at 8.

[556] Sprint Comments at 53.

[557] AT&T Reply at 35-36.

[558] TCI Comments at 30-31; TRA Comments at 23. *See also* Washington Commission Comments at 8; AT&T Reply at 24-25.

[559] CompTel Reply at 8-11.

[560] AT&T Comments at 22-24; AT&T Reply at 17-18.

the benefits of TELRIC-based access rates would outweigh those administrative burdens.[561] USTA asserts that the rate prescription suggested by AT&T would recreate rate-of-return regulation, and that its detrimental effects would outweigh the administrative benefits alleged by AT&T.[562] PacTel argues that every error in the estimation of costs used to set prices (both over- and under-estimation) will work to the advantage of entrants since they can choose in each individual case whether to pay for the facilities or resell the services and pay the below-cost access charges.[563] The Florida Commission recommends against adopting prescriptions that would preclude incumbent LECs from lowering prices where competitive conditions warrant it.[564]

164. AT&T denies that adopting a TSLRIC pricing standard would create a serious common cost allocation problem, because both unbundled network elements and access rate elements correspond to network facilities to a great extent.[565] The Texas Commission argues that it would be easy to develop a reasonable overhead loading factor based on the ratio of overhead costs to revenues, and that use of a single overhead loading factor eliminates the need to develop common cost allocation factors.[566] AirTouch observes that TSLRIC raises common cost allocation issues, and maintains that we must take into account the extent of competition and the different demand elasticities of different services when we address these common cost allocation issues. AirTouch questions whether "a minute is a minute" pricing is necessarily the best means to allocate common costs.[567] Similarly, API argues that the common cost allocation to any particular service should be limited to the amount of common costs that could be recovered in a competitive market.[568] State Consumer Advocates argue that any forward-looking economic cost method should permit incumbent LECs to recover a reasonable allocation of joint and common costs, including joint and common costs associated with the local loop.[569]

---

[561] AT&T Reply at 17-18.

[562] USTA Reply at 47 and Attachment 2 at 50.

[563] PacTel Comments at 36.

[564] Florida Commission Comments at 4-5.

[565] AT&T Comments at 24-25.

[566] Texas Commission Comments at 28-29.

[567] AirTouch Comments at 7-9. *See also* Ameritech Reply, Attachment A at 10.

[568] API Comments at 26.

[569] State Consumer Advocates Comments at 7-13, 54-55.

b. Reinitialization of PCIs on a Rate-of-Return Basis

165. A number of incumbent LECs argue that reinitializing indexes on the basis of earnings would adversely affect the efficiency incentives of price cap regulation.[570] In particular, PacTel and USTA note that the Commission has criticized earnings-based PCI adjustments in the past, and is contemplating eliminating sharing, because sharing is based on earnings, in the *Price Cap Fourth Further NPRM*.[571] Frontier asserts that represcribing the authorized rate of return would leave other causes of uneconomic access charges unaddressed.[572] GSA/DOD argues that, contrary to the incumbent LECs, the Commission did not want to sever rates from costs when it adopted price cap regulation, because it retained the sharing requirement.[573] Ad Hoc argues that reinitializing rate levels at 11.25 percent, or some other rate of return, would be administratively easy, and that the rate structure rule revisions contemplated in Section III of the NPRM are adequate to ensure that prices of individual services are efficient.[574] API maintains that it is important to reduce rates to cost as soon as possible, and so recommends represcribing the authorized rate of return and reinitializing PCIs on that basis.[575]

166. USTA opposes represcribing the authorized rate of return, because the 1996 Act has created uncertainty regarding the incumbent LECs' cost of capital, and because interest rates have not changed greatly over the past 10 months.[576] USTA also claims that no one has provided adequate reason to reduce the authorized rate of return, and predicts that the cost of capital would increase as the competition faced by incumbent LECs increases.[577] USTA asserts that represcribing the authorized rate of return would adversely affect small incumbent LECs.[578] MCI contends that its submission in the *Preliminary Rate of Return Inquiry* supports

---

570 USTA Comments at 17; BellSouth Comments at 47-48; USTA Reply at 46-47.

571 PacTel Comments at 37-38; USTA Reply, Attachment 2 at 43.

572 Frontier Comments at 13.

573 GSA/DOD Reply at 12-13. *See also* MCI Reply at 7-8.

574 Ad Hoc Comments at 41-45.

575 API Comments at 27; API Reply at 8-9, 18. *See also* CPI Comments at 23.

576 USTA Comments at 16-17.

577 USTA Reply, Attachment 13 at 3-8.

578 USTA Comments at 16-17.

reducing the authorized rate of return to 10 percent.[579] USTA claims that MCI bases its represcription recommendation on incorrect calculations.[580] BA/NYNEX maintains that there is no basis in this record for represcribing the authorized rate of return, and argues that a represcription proceeding would be burdensome.[581] PacTel cites the *Preliminary Rate of Return Inquiry NPRM* for the Commission's observation that rate of return prescriptions have little relevance to price cap carriers, and argues that they do not trigger decreases in the price cap indices.[582]

167. GSA/DOD recommends represcribing the authorized rate of return and reinitializing PCIs on that basis, because it believes earnings of carriers under price cap regulation has been excessive.[583] BA/NYNEX opposed a rate-of-return-based reinitialization in its comments,[584] but revised its position in an *ex parte* statement submitted on April 4, 1997. In particular, BA/NYNEX stated that it reached agreement with AT&T on a comprehensive proposal on universal service and access reform that includes, among other things, a reinitialization based on a rate-of-return of 11.25 percent.[585] USTA denies that incumbent LECs have overearned under price cap regulation, and asserts that the incumbent LECs' "economic rate of return" was 8.75 percent from 1991 to 1995.[586] According to SWBT, arguments for decreasing the rate of return are based on non-forward-looking

---

579 MCI Comments at 25.

580 USTA Reply at 47-48 and Attachment 13.

581 BA/NYNEX Comments at 25-26.

582 PacTel Comments at 43-44, *citing* Public Notice, Common Carrier Bureau Sets Pleading Schedule in Preliminary Rate of Return Inquiry, 11 FCC Rcd 3651 (Com.Car.Bur., Accounting and Audits Div., 1996).

583 GSA/DOD Comments at 13-15; GSA/DOD Reply at 9-10.

584 BA/NYNEX Comments at 24-27.

585 Letter from G.R. Evans, Vice President, Federal Regulatory Affairs, NYNEX, to William Caton, Secretary, FCC, April 4, 1997.

586 USTA Comments at 18 and Attachment 4; USTA Reply at 46. *See also* SWBT Reply at 41. USTA claims that the current rate-of-return prescription of 11.25 percent is an accounting measure rather than an economic measure, and therefore inherently less accurate, because accounting rates of return are based on accounting rather than economic depreciation, book values rather than economic values, and accrued revenues and expenses rather than cash flows. USTA Comments, Attachment 4 at 2. USTA bases its determination of the economic rate of return on values of certain categories of telecommunications equipment as collected by the Bureau of Economic Analysis (BEA), and on dividend payments of the incumbent price cap LECs. USTA Comments, Attachment 4 at 5 and Schedule 1.

accounting measures that do not accurately measure the incumbent LECs' cost of capital.[587] GTE asserts that the authorized rate of return is too low to reflect the risks faced by incumbent LECs now that they face competition.[588] Ad Hoc argues that services subject to effective competition should be removed from price cap regulation, and that the authorized rate of return should be lowered to reflect the lower risk associated with the services that remain subject to price cap regulation.[589]

d. Reinitialization of PCIs on a TSLRIC Basis

168. Some incumbent LECs argue that reinitializing PCIs using TSLRIC would be equivalent to abandoning price cap regulation in an arbitrary and confiscatory manner.[590] Similarly, BellSouth and BA/NYNEX contend that reinitializing PCIs at TELRIC or TSLRIC levels would destroy price cap regulation by recreating the link between rates and costs.[591] BellSouth and USTA claim that price cap regulation has worked very well, and there is no justification for eliminating it.[592] BellSouth also notes that the Commission rejected proposals to revert to cost-of-service regulation in the *LEC Price Cap Performance Review Order*.[593]

169. Ad Hoc recommends reinitializing PCIs to equate with the aggregation of revenues from individual services priced at TSLRIC.[594] Although API supports TSLRIC, it opposes reinitializing indices on a TSLRIC basis because of the time needed to conduct a TSLRIC study.[595] The Florida Commission argues that we could require incumbent LECs to begin reducing their access rates gradually while we are conducting cost studies necessary to calculate TSLRIC levels.[596] MCI maintains that we must "reinitialize" APIs and SBIs, as well

---

[587] SWBT Reply at 43-45.

[588] GTE Comments at 77.

[589] Ad Hoc Comments at 70.

[590] PacTel Comments at 39; GTE Comments at 75-76; USTA Reply at 46-47 and Attachment 2 at 43, 48.

[591] BellSouth Comments at 45; BellSouth Reply at 30-31; BA/NYNEX Comments, Attachment 1 at 8-9. *See also* USTA Reply, Attachment 3 at 17.

[592] BellSouth Reply at 31-34; USTA Reply at 12-13.

[593] BellSouth Reply at 32, *citing LEC Price Cap Performance Review Order*, 10 FCC Rcd at 8973.

[594] Ad Hoc Comments at 70.

[595] API Comments at 27.

[596] Florida Commission Comments at 5.

as PCIs, to ensure that rates under price cap regulation are at economic cost-based levels.[597]

170. A number of parties argue that proxy models provide only hypothetical and averaged costs, and therefore are not representative of the costs incurred by actual individual carriers, and in particular the costs incurred by small carriers.[598] According to USTA, unless rates are based on actual network costs, rates will not reflect accurately the opportunity costs of using the network.[599] According to PacTel, the proxy models are designed to calculate differences in the costs of serving different geographic areas, not actual costs. Because no one has proposed deaveraging access rates on the basis of Census Block Groups, as measured in the proxy models, PacTel claims that there is no reason to base access rates on the results of the proxy models.[600] Similarly, the Texas Commission questions whether TSLRIC proxy models would produce accurate company-specific costs, as opposed to industry-wide averaged costs. The Texas Commission, therefore, supports TELRIC as a pricing standard for access rates.[601] PacTel contends that the proxy models do not place sufficient weight on traffic volume, which PacTel asserts influences costs more than population density or other factors reflected in the models.[602] Southwestern Bell claims that the network assumed by the Hatfield model could not be used to provide service.[603] Southwestern Bell also claims that it has not been able to replicate the results of the Hatfield Model reported by MCI.[604]

171. Airtouch observes that TSLRIC raises common cost allocation issues, and maintains that we must take into account the extent of competition and the different demand elasticities of different services when we address these common cost allocation issues. Airtouch questions whether "a minute is a minute" pricing is necessarily the best means to allocate common costs.[605] Similarly, API argues that the common cost allocation to any

---

[597] MCI Comments at 19-24.

[598] Evans, *et al.* Comments at 5-6; TDS Reply at 10-14; Rural Tel. Coalition Reply at 16-17; Minnesota Independent Association Reply at 6; USTA Reply at 14. *See also* PacTel Comments at 36-37; PacTel Reply at 10-11; PacTel Reply, Egan Aff. at 23-24; BA/NYNEX Reply at 14.

[599] USTA Reply, Attachment 2 at 23-24, Attachment 3 at 1.

[600] PacTel Comments at 33-34. *See also* Rural Tel. Coalition Reply at 15-17.

[601] Texas Commission Comments at 26-27.

[602] PacTel Comments at 34-35; PacTel Reply, Egan Aff. at 26-27.

[603] SWBT Reply at 25.

[604] SWBT Reply at 25-27. *See also* USTA Reply, Attachment 3 at 6.

[605] AirTouch Comments at 7-9. *See also* Ameritech Reply, Attachment A at 10.

particular service should be limited to the amount of common costs that could be recovered in a competitive market.[606] On the other hand, the Texas Commission argues that it would be easy to develop a reasonable overhead loading factor based on the ratio of overhead costs to revenues, and that use of a single overhead loading factor eliminates the need to develop common cost allocation factors.[607] State Consumer Advocates argue that any forward-looking economic cost method should permit incumbent LECs to recover a reasonable allocation of joint and common costs, including joint and common costs associated with the local loop.[608] AT&T denies that adopting a TSLRIC pricing standard would create a serious common cost allocation problem, because both unbundled network elements and access rate elements correspond to network facilities to a great extent.[609]

172. Some state commission oppose the FCC's proposal to place responsibility for cost studies on state commissions, because it would create excessive demands on scarce state commission resources.[610] The Kansas Commission argues that state commissions do not have expertise in reviewing interstate costs.[611] The Florida and Oregon Commissions question whether we have authority under the Communications Act to adopt this proposal.[612] The Florida and Georgia Commissions question whether the FCC would permit different pricing standards for interstate access to be adopted in different states.[613] The Texas Commission recommends giving states the option of reviewing incumbent LEC cost studies.[614] Rather than this Commission directing the states to conduct cost studies, the California Commission recommends permitting state commission to permit the cost studies that they have already begun, and relying on the results of those studies.[615]

---

[606] API Comments at 26.

[607] Texas Commission Comments at 28-29.

[608] State Consumer Advocates Comments at 7-13, 54-55.

[609] AT&T Comments at 24-25.

[610] Illinois Commission Comments at 23-24; Kansas Commission Comments at 5-6; Oregon Commission Comments at 3-4; Georgia Commission Reply at 4-5.

[611] Kansas Commission Comments at 5-6.

[612] Florida Commission Comments at 9; Oregon Commission Comments at 4. *See also* BellSouth Comments at 46-47; NCTA Comments at 22.

[613] Florida Commission Comments at 9; Georgia Commission Reply at 4-5.

[614] Texas Commission Comments at 27-28.

[615] California Commission Comments at 12-13.

e. Policy-Based X-Factor Increase

173. Cable and Wireless supports increasing the X-Factor in equal increments over a five-year period to drive rates to TSLRIC levels.[616] MCI suggests increasing the CPD for each price cap LEC for five years, by the ratio of that carrier's PCI to its API, to eliminate that carrier's headroom.[617] A number of commenters recommend increasing the X-Factor in addition to requiring a reinitialization, to ensure that access rates remain at long-run incremental cost levels.[618] Frontier opposes relying exclusively on an increased X-Factor to force access rates to cost, because it would not affect current rates.[619] Frontier, alternatively, argues that any X-Factor would double-count the TSLRIC-based reinitialization it supports, and so recommends eliminating the X-Factor from the price cap formula after the reinitialization.[620]

174. BellSouth claims that the current 0.5 percent CPD has "outlived its usefulness," and BellSouth and GTE oppose increasing the CPD as an arbitrary and confiscatory measure.[621] SNET claims that increasing the X-Factor merely because the price cap LECs have earned too much, or simply to drive rates down, is essentially an abandonment of price cap regulation, because it would punish incumbent LECs for their efficiency gains made under the price cap regime.[622] BA/NYNEX and GTE contend that the X-Factor should reflect reasonably expected incumbent LEC productivity growth rather than to achieve a specific rate reduction.[623]

175. SNET argues that increasing the X-Factor to force access rates down would not result in a more competitive market, and that treating all price cap carriers the same would

---

[616] Cable and Wireless Comments at 28-29. *See also* NCTA Comments at 21-22; WorldCom Comments at 91.

[617] MCI Comments at 28.

[618] AT&T Comments at 69-70; ACTA Comments at 21; GSA Reply at 14-15. *See also* WorldCom Comments at 91 (increasing X-Factor is necessary to reflect incumbent LEC productivity growth); TRA Comments at 23 (recommending an X-Factor increase following prescription of new access rates); CPI Comments at 23-25 (reinitialize indices and increase the X-Factor prior to permitting any market-based reforms).

[619] Frontier Comments at 13.

[620] Frontier Comments at 12 n.22.

[621] BellSouth Comments at 49; GTE Comments at 77-78.

[622] SNET Reply at 23-24. *See also* BA/NYNEX Reply at 32-33.

[623] BA/NYNEX Reply at 30; GTE Reply at 26-27.

disregard fundamental differences in scale and scope, and differences in regional economics between small and midsized elective price cap incumbent LECs on one hand, and the RBOCs and GTE on the other.[624] PacTel argues that increasing the X-Factor would force access rates down in both urban and rural areas, and so would discourage competitive entry in rural areas.[625] PacTel argues that the price reductions caused by the productivity factor perversely apply productivity reductions, which are supposed to replicate competition, to services where prices have already fallen because of actual competition.[626] PacTel recommends resolving price cap issues in other pending proceedings rather than using price cap regulation as a device to lower access rates to levels PacTel considers confiscatory.[627]

C. Equal Access Costs

176. AT&T, NCTA, Sprint, and WorldCom recommend a exogenous cost decrease to remove equal access costs from the incumbent price cap LECs' PCIs.[628] AT&T estimates that equal access costs constitute an annual $110 million dollar subsidy for the LECs.[629] AT&T argues that the Commission previously found that failure to make a downward adjustment would be unfair to ratepayers and perpetuate an implicit cross-subsidy. In light of this, AT&T argues that the Commission should now make a downward adjustment to account for the completion of the amortization of those costs. Sprint argues that without such an adjustment, incumbent LECs would be able to impose charges for other rate elements to recover costs that simply no longer exist. Sprint contends that most of the equal access costs are in the local switching basket, requiring that basket's price cap index to be reduced. To the extent that other baskets were affected, Sprint contends that the appropriate PCI reductions

---

[624] SNET Comments at 28-30.

[625] PacTel Comments at 40. PacTel claims to be more subject to harm from the productivity factor than any other LEC because a few highly competitive central offices account for over 75 percent of its traffic, leaving it highly reliant on intraLATA toll services. According to PacTel, intraLATA toll services have become increasingly competitive in California, leaving it unable to invest in its network because of artificial productivity factors. *Id.*

[626] PacTel Comments at 41-42.

[627] PacTel Comments at 39.

[628] AT&T Comments at 68-69; NCTA Comments at 28; Sprint Comments at 59; WorldCom Comments at 94. *See also* New York Commission Comments at 1 (supporting the removal of equal access costs from access charges).

[629] AT&T Comments, Appendix F (using 1990 Annual Interstate Access Filings of BOCs, AT&T calculates 1990 revenue associated with non-capitalized equal access expenditures and converts to a present day annual revenue estimate by comparison to difference between initial Traffic Sensitive Basket price cap index to 1996 Traffic Sensitive Basket price cap index).

should be made.[630] The Georgia Commission recommends that the Commission verify whether equal access costs continue to be reflected and, if so, make the appropriate adjustments to account for these costs.[631]

177. The BOCs argue that there should be no exogenous cost decrease to account for completion of the amortization of equal access costs.[632] BellSouth argues that, given the Commission's decision not to grant an exogenous increase for these costs during price cap initialization, it would be unfair to require an exogenous decrease now.[633] PacTel and USTA argue that price cap regulation has historically treated equal access costs as endogenous. According to PacTel and USTA, it would be arbitrary to change that treatment for some equal access costs and not others.[634] USTA, Ameritech, and SWBT argue that the Commission has addressed this matter before and correctly concluded that no exogenous treatment was warranted.[635] BellSouth argues that just as in the *LEC Price Cap Performance Review Order*, 10 FCC Rcd at 9094-9095, there is insufficient support for requiring LECs to make an exogenous decrease based on the complete amortization of equal access costs.[636] USTA and SWBT argue that LECs continue to incur new equal access costs that have not been recovered, such as when a LEC must purchase equal access software for a new digital switch.[637]

178. TCA argues that some small LECs have not received a *bona fide* request to convert to equal access. TCA contends that when these LECs make the conversion, they should be allowed the same treatment of their equal access costs as other LECs.[638] Similarly, GCI raises the issue of those LECs that have not converted to equal access. GCI recommends that these LECs be allowed to recover their costs through the Local Switching rate element,

---

630 Sprint Comments at 59.

631 Georgia Commission Reply at 41.

632 Ameritech Comments at 54-55; BA/NYNEX Comments at 66; PacTel Comments at 24-25; SWBT Comments at 62; USTA Comments at 85.

633 BellSouth Comments at 88. *See also* BA/NYNEX Comments at 66.

634 PacTel Comments at 24-25; USTA Comments at 49. *See also* SWBT Reply at 43.

635 *See, e.g.*, USTA Comments at 85; Ameritech Comments at 55; SWBT Reply at 41.

636 BellSouth Comments at 87.

637 USTA Comments at 49; SWBT Reply at 42.

638 TCA Comments at 5-6.

rather than a general allocation.[639]

D. Correction of Improper Cost Allocations

1. Marketing Expenses

179. Incumbent LECs and AT&T agree that marketing expenses are inappropriately allocated to the interstate jurisdiction.[640] USTA notes that the net effect of the Commission's decision to include access revenues in the allocation factor for marketing expenses in the *Marketing Expense Reconsideration Order*[641] was to allocate approximately 26 percent of incumbent LECs' total marketing expenses to the interstate jurisdiction.[642] USTA argues that incumbent LECs must be afforded an opportunity to recover the interstate portion of marketing expenses, which it estimates to be $2.2 billion for price cap LECs and $2.4 billion for all incumbent LECs.[643] SWBT estimates that $100 million of its marketing-related costs are allocated to interstate services and recommends that marketing costs be recovered through a public policy element until separations reform can be completed.[644] Based on 1995 data, GTE estimates that the separations process allocates $84.6 million of its marketing expenses to the interstate jurisdiction.[645]

180. AT&T estimates that inappropriate end user retail expenses recovered through interstate switched carrier access total $840.2 million -- approximately $575 million in direct retail expenses including marketing and customer service costs, and $265 million in indirect retail expenses including general support, corporate operations, and uncollectible revenue.[646] AT&T argues that because access is a wholesale service, not a retail service, this implicit

---

[639] GCI Comments at 8.

[640] *See, e.g.*, SWBT Comments at 8-9; AT&T Comments at 66-67, Appendix D; *cf.* GTE Comments at 42 (proposing that incumbent LECs prepare separations-based cost studies to show the amount of marketing expense erroneously assigned to the interstate jurisdiction to be used to compute the separations and TIC-related components of a regulatory policy charge).

[641] *Marketing Expense Reconsideration Order*, 2 FCC Rcd at 5353.

[642] USTA Comments, Attachment 2 at 25.

[643] USTA Comments at 79-80, Attachment 16 at 4.

[644] SWBT Comments at 8-9.

[645] GTE Reply at 8.

[646] AT&T Comments at 66.

subsidy contained in access charges is improper for three reasons.[647] First, recovery of retail expenses through access charges violates section 252(d)(3) of the Act,[648] which states that wholesale rates will be determined on the basis of retail rates, excluding the portion attributable to marketing, billing, collection, and other costs that will be avoided by the LEC.[649] Second, inclusion of retail costs in access charges violates the fundamental principle that services that should be priced at their long-run incremental cost, resulting in cross-subsidies from access charges to other services.[650] Finally, inclusion of retail costs in access charges violates cost-causation principles, which state that retail costs should be borne by those who cause them, *i.e.*, retail end users.[651]

181. AT&T and WorldCom propose that, pending separations reform that reallocates retail marketing costs to the intrastate jurisdiction, the Commission reassign recovery of such costs from interstate access charges to end users.[652] AT&T's proposal would recover these costs from business lines and non-primary residential lines, but not from primary residential lines.[653] The Rural Tel. Coalition opposes recovery of such costs from end users.[654] USTA contends that, until the separations rules are changed, incumbent LECs should continue to recover these costs in current access prices and that the marketing expense allocated to common line should remain in common line.[655]

[647] AT&T Comments at 66-67; *cf.* New York Commission Comments at 3 (arguing that retail costs allocated to the interstate jurisdiction that are avoided when competitors resell incumbent LECs' services should be reflected in lower access charges).

[648] 47 U.S.C. § 252(d)(3).

[649] AT&T Comments at 66-67.

[650] AT&T Comments at 67.

[651] AT&T Comments at 67.

[652] AT&T Comments at 53; WorldCom Comments at 71; *see also* Letter from Bruce K. Cox, Vice President, Government Affairs, AT&T, to William F. Caton, Acting Secretary, Federal Communications Commission, March 19, 1997.

[653] Letter from Bruce K. Cox, Vice President, Government Affairs, AT&T, to William F. Caton, Acting Secretary, Federal Communications Commission, March 19, 1997.

[654] Rural Tel. Coalition Reply at 5-6.

[655] USTA Comments at 80.

2. General Support Facility Costs

182. AT&T and WorldCom assert that the Commission should not permit incumbent LECs to recover in access charges the costs caused by the LECs' detariffed billing and collection functions, including those arising from use of GSF and computer costs in providing those functions.[656] According to AT&T's study, $124 million of expenses recovered in interstate access support the nonregulated billing and collection category.[657] Of the $124 million, $60.1 million is included in interstate switched carrier access, and $20.5 million is in interstate special carrier access, with the remainder recovered by the SLC.[658] WorldCom recommends that the Commission correct the Part 32 USOA rules for regulated costs and Part 64 allocation rules to remove this investment from access charges, and should require corresponding reductions in the TIC.[659]

V. ACCESS REFORM FOR INCUMBENT RATE-OF-RETURN LOCAL EXCHANGE CARRIERS

183. The majority of commenters agree generally with our conclusion to limit the scope of this proceeding to price cap LECs.[660] Many parties are concerned, however, about the impact decisions made in this proceeding may have on some rate-of-return LECs, and urge the Commission to consider the needs of small to mid-sized and rural rate-of-return incumbent LECs when adopting proposals in this proceeding.[661]

184. Cincinnati Bell, ALLTEL, and ITTA oppose delaying access reform for non-price cap LECs.[662] Centennial states that it prefers that the Commission apply its access

[656] AT&T Comments at 67, Reply at 34; WorldCom Comments at 71 (proposing that the costs of non-regulated services be removed from the TIC).

[657] AT&T Comments at 67-68, Appendix E.

[658] AT&T Comments, Appendix E at 2.

[659] WorldCom Comments at 71.

[660] *See, e.g.*, Alaska Telephone Association Comments at 3; Frederick & Warinner Comments at 3; NECA Comments at 2; TCA Comments at 2; Sprint Comments at 9; WITA Comments at 2; GSA/DOD Comments at 13.

[661] *See, e.g.*, Staurulakis Comments at 2; GCI Comments at 1-4, Reply at 5-6; Alaska Telephone Association Comments at 3; Rural Tel. Coalition Comments at 2-3; TDS Comments at 6-7; GVNW Comments at 4, Reply at 3; Western Alliance Comments at 1-3.

[662] Cincinnati Bell Comments at 2; ALLTEL Comments 3, 5-7, Reply at 3; ITTA Comments at 4.

reforms to *all* incumbent LECs, subject to an appropriate waiver for small, rural LECs whose special circumstances warrant special accommodation, but that at a minimum, the Commission should apply all of its access reforms to all Tier 1 LECs.[663] Centennial argues that a large, Tier 1 LEC, such as PRTC, that already faces active competition from competitive carriers should not be exempt from the new access reform rules.[664]

185. Many commenters stress the need for immediate or prompt access reform for rate-of-return LECs. They contend that rate-of-return LECs are facing increasing competitive pressures and need the ability to respond to changes in the market.[665] Roseville and Frontier recommend that the Commission distinguish between rural and non-rural carriers.[666] Frontier argues that smaller price cap carriers are more similarly situated to non-price cap rural carriers than they are to non-rural carriers and urges the Commission to temporarily exempt all rural LECs, price cap and non-price cap, from the rules adopted in this proceeding.[667] Citizens contends that some of the approaches proposed in the NPRM are not appropriate for price cap LECs that primarily serve rural areas and have a low proportion of business lines.[668] Other commenters assert that rural LECs have a lower percentage of low-cost/high-margin customers, that their access charge revenues represent a higher percentage of their total revenues than they do for the average regional BOC, and that the loss of even a small number of customers can result in a much higher proportionate loss of revenue when compared to the markets of typical price cap LECs.[669]

186. For these reasons, some commenters argue that non-price cap LECs need regulatory flexibility and the option of adopting the rate structure changes required for price-cap LECs in this proceeding.[670] NECA, for example, states that because NECA pool carriers' rates represent a wide variety of markets with disparate cost characteristics, the Commission

[663] Centennial Cellular Corporation Comments 2-3.

[664] *Id.* at 6-7.

[665] *See, e.g.*, ALLTEL Comments at 3, 5-7, Reply at 3; Cincinnati Bell Telephone Comments at 2- 3; Roseville Tel. Comments at 6-7, Reply at 4-10; GVNW Comments at 4; ITTA Comments at 4.

[666] Roseville Tel. Comments at 2; Frontier Comments at 5-6 n. 10.

[667] Frontier Comments at 5-6 n. 10.

[668] Citizens Utilities Comments at 3-6, 13-14.

[669] *See, e.g.*, GVNW Comments at 3-4; ALLTEL Comments at 15.

[670] *See, e.g.*, Aliant Reply at 4-5; ALLTEL Comments at 4, 8, Reply at 3-4; Minnesota Independent Coalition Comments at 2; ITTA Comments at 4; TDS Comments at 10-12, 16, Reply at 4-6; NECA Comments at 9-10, Reply at 6; Roseville Tel. Comments at 2.

should permit these carriers to have the regulatory flexibility to select and implement rate structure changes adopted in this proceeding pending completion of the separate rate-of-return proceeding.[671]

VI. OTHER ISSUES

A. Application of Part 69 to Unbundled Network Elements

187. Several incumbent LECs disagree with our tentative conclusion to exclude from unbundled network elements the application of Part 69 access charges. PacTel argues that access charges should not be excluded from the sale of unbundled network elements because such charges include subsidies for universal service. Competitors, PacTel argues, will have an economic incentive to purchase unbundled elements to avoid access charges, undermining support for universal service until an explicit universal service funding mechanism is adopted.[672] SBC contends that the Commission has recognized legitimate costs that are recovered through access charges. Recovery of these costs will be reduced if the Commission allows purchasers of unbundled elements to pay substantially less on a per minute basis than they would through interconnection arrangements. SBC estimates that excluding access charges from the sale of unbundled network elements could jeopardize its recovery of $705 million in end user common line loop costs and $683 million in switched access costs based on SBC's 1996 switched access demand levels.[673] USTA contends prices for unbundled elements should include access charges to ensure embedded costs assigned to the interstate jurisdiction are recovered to the extent network elements are used to provide interstate services.[674]

188. Other incumbent LEC commenters argue that rebundling network elements is equivalent to offering access services and justifies the imposition of access charges. BellSouth, for example, contends that access charges should apply to competitors that rebundle network elements because rebundled elements constitute an underlying retail service and access charges are applicable when services are purchased for retail sale.[675] PacTel suggests that access customers will perceive unbundled elements as a substitute for access service. By excluding access charges from the sale of unbundled elements, PacTel contends, the Commission would sanction a violation of Section 202(a) of the Communications Act

[671] NECA Comments at 9-10, Reply at 6.

[672] PacTel Comments at 55-57. *See also* GVNW Comments at 5.

[673] SBC Comments at 51-52.

[674] USTA Comments at 54-55.

[675] BellSouth Comments at 13.

which prohibits unreasonable discrimination in charges for similar services.[676]

189. Smaller LECs whose rates are set under rate-of-return regulation advocate the imposition of access charges on unbundled network elements because a substantial portion of their revenues are derived from state and interstate access charges.[677] Roseville Telephone argues that, absent the imposition of access charges on the sale of unbundled network elements, incumbent LECs will not recover the costs of their underlying facilities because TELRIC prices will not recover costs attributable to federal-state separations policies and a portion of the incumbent LEC's embedded costs.[678]

190. IXCs support the Commission's tentative conclusion to exclude unbundled network elements from Part 69 access charges. Excel agrees with the Commission's rationale that carriers purchasing unbundled elements at cost-based rates have already compensated incumbent LECs for the ability to originate and terminate calls, rendering further compensation unnecessary.[679] Sprint also supports the exclusion of access charges from unbundled network elements, arguing that adding access charges to cost-based prices for unbundled elements would undermine the pro-competitive purpose of the 1996 Act. To the extent prices for unbundled elements do not recover universal service costs, Sprint argues that the Commission should remove implicit subsidies from access charges and have all service providers contribute to universal service through a competitively neutral funding mechanism.[680] Sprint also challenges the view of LEC commenters that rebundling network elements is the equivalent of offering a retail service. According to Sprint, when elements are used to originate and terminate calls, the purchaser of the unbundled elements, rather than the incumbent LEC, is offering exchange services using those facilities. Imposing access charges on unbundled elements, Sprint argues, would be similar to having the purchaser of an automobile pay rental fees in addition to the purchase price simply because the automobile is used for transportation whether it is purchased or leased.[681]

---

676 PacTel Reply at 8-10. *See also* GVNW Comments at 4-5.

677 Frederick and Warriner Comments at 4 (stating that 60% of revenues generated by small LECs it represents are derived from state and interstate access charges).

678 Roseville Telephone comments at 13-14.

679 Excel Comments at 7.

680 Sprint Reply at 7.

681 *Id.* at 6.

B. Treatment of Interstate Information Services

191. *Non-cost-based rates.* ISPs, consumers, and several consumer groups applaud the Commission's tentative conclusion to not require ISPs to pay access charges and urge us to make it our final decision.[682] These commenters state that the current access charge framework consists of non-cost-based rates, that it was designed to address rate discrimination in the interexchange market, as well as to preserve subsidy flows between local and long distances services. They argue that this regime should not be extended to ISPs.[683] Internet Access Coalition states that there is no justification for requiring ISPs to pay charges designed to recover the cost of network features and functions that were designed for voice traffic, features that ISPs neither want nor need.[684]

192. Consumer groups and other commenters assert that the imposition of non-cost-based access fees would diminish consumer use of the Internet and other information services.[685] MAP, *et al.,* claims that usage-based fees might be passed on to consumers, which could diminish total use of the Internet and especially limit use by lower-income citizens.[686]

193. America On-Line states that access charges are inappropriate for ISPs, regardless of whether they consist of non-cost-based rates or are priced at forward-looking costs. America On-Line contends that no matter how access charges are established, they do not and

---

682 *See, e.g.,* American Library Association Comments at 1; MAP, *et al.* Comments at 3; Radoff Comments at 1; Lyman C. Welch Comments at 1; Colorado Library Education and Healthcare Telecommunications Coalition Reply at 1; Gallegos Comments at 2; California Commission Reply at 7; NCTA Comments at 2; America On-Line Comments at 4; CIEA Comments at 3; CompuServe\Prodigy Comments at 4; Information Industry Association Comments at 1-2; Internet Access Coalition at 10-13; Microsoft Comments at 3-4; Minnesota Internet Services Trade Association Comments at 1; Newspaper Association of America Reply at 1; Alarm Industry Communications Committee Reply at 1.

683 *See, e.g.,* America On-Line Comments at 9; Internet Access Coalition Comments 10-13; American Library Association Comments at 1; NCTA Reply at 10-11.

684 Internet Access Coalition Comments at 6.

685 *See, e.g.,* MAP, *et al.* Comments at 3-4; Ozarks Technical Community College Comments at 1; Colorado Library and Healthcare Telecommunications Coalition Reply at 1; Gallegos Comments at 2; CompuServe\Prodigy Reply at 4; PSINet Reply at 9-10; Alarm Industry Communications Committee Reply at 4-6. We received over 300,000 comments from consumers via our electronic mailbox. These commenters overwhelmingly oppose the imposition of access charges on ISPs. Most insist that many consumers will be unable to afford using the Internet if ISPs are required to pay access charges and those charges are then passed on to consumers.

686 MAP, *et al.* Comments at 4.

should not apply to ISPs because ISPs are not carriers.[687] America On-Line states that as providers of information services, ISP fall squarely outside of the definition of "telecommunications carriers" as defined in the 1996 Act.[688] Several commenters claim that ISPs are end-users of telecommunications services, and the manner in which they use the local network supports the conclusion that they are end users rather than carriers.[689]

194. Most LECs and a few other commenters call for the imposition of access charges on ISPs.[690] They state that ISPs currently do not pay for their portion of local exchange switching facilities assigned to the interstate jurisdiction.[691] BA/NYNEX states that current usage levels can only be accommodated on the circuit switched network by continuous investment in more network capacity, however, LECs are not recovering their investment under the current pricing structure for ISPs.[692] Some LECs acknowledge that the current framework of access charges should not be applied to ISPs, but rather, ISPs should be charged usage-sensitive "reformed" access charges which do not contain non-cost-based subsidies.[693]

195. PacTel contends that ISPs are not like other business customers, because they do not use local business lines for a mix of originating and terminating calls, and, thus, do not pay outbound usage charges.[694] PacTel further claims that ISPs' current service architectures, while using business lines, look strikingly like the other common carriers' serving arrangements prior to the divestiture of AT&T. According to PacTel, ISPs gain access to LEC loops and switches in order to offer services to end users across all major population centers, just as IXCs do. Further, ISPs do not terminate calls, but provide connection to the Internet or on-line services.[695]

---

687 America On-Line Reply at 6.

688 *Id.*

689 *Id.* at 5; *see also,* Information Industry Association Comments at 3; Internet Access Coalition Comments at 10-13; Pennsylvania Internet Service Providers Comments at 21.

690 BA/NYNEX Comments at 64; PacTel Comments at 74; SONETECH Comments at 19; USTA Comments at 83; U S West Comments at 83; GTE Comments at 18; GCI Comments at 8.

691 *See, e.g.,* U S West Reply at 42; BA/NYNEX Comments at 64; USTA Comments at 82.

692 BA/NYNEX Comments at 62; *see also,* PacTel Comments at 76-77.

693 PacTel Reply at 6; *see also,* USTA Comments at 84; AT&T Comments at 71-72.

694 PacTel Reply at 27-28.

695 *Id.*

196. *Implicit subsidy for ISPs.* USTA and several LECs claim that current flat rate pricing schemes for ISPs create an implicit subsidy for ISPs, because the flat rate charges ISPs pay fail to pay for the network resources they use.[696]

197. Compuserve and Prodigy state that the rates for flat-rated business lines used by ISPs already cover their costs, and in some jurisdictions, they provide a subsidy for below cost local exchange residential services.[697] Compuserve and Prodigy assert that regional BOC (RBOC) studies underestimate the revenues the RBOCs are currently receiving from ISP use of business lines.[698]

198. Several ISPs and consumer groups point to the increase in LEC revenues due to increased demand for new telecommunications services associated with ISPs.[699] Most significantly, commenters cite the increase in consumer demand for second lines. Internet Access Coalition refers to an ETI Study [need cite] which found that increased revenue from residential second lines used primarily or exclusively to access on-line services exceeds the increased incumbent LEC costs attributable to the growth of these services by a factor of six-to-one.[700] Internet Access Coalition challenges PacTel's conclusion that the costs of second lines exceed the flat rate charged by Pacific Bell for those lines. Internet Access Coalition states that several incumbent LECs, including PacTel, have, in other forums, expressly attributed their recent high earnings to the surge in demand for second lines.[701]

199. *Network congestion.* Several commenters, most of them incumbent LECs, claim that current network congestion problems are the result of the current pricing policies which allow ISPs to pay flat rates for usage sensitive services.[702] USTA states that congestion caused by ISPs raises network reliability concerns and delays the introduction of new

---

696 USTA Comments at 82-83; *See, e.g.,* U S West Comments at 83-84; GVNW Comments at 15; ACTA Comments at 24-30.

697 CompuServe/Prodigy Comments at 12.

698 *Id.* CompuServe/Prodigy states that it now pays the LECs almost $36 million on an annual basis for the approximately 85,000 local business lines it employs to make available its services to subscribers (85,000 lines x $35 per month per line x 12 months = $35,700,000).

699 *See, e.g.,* Consumer Project Reply at 3; Internet Access Coalition Comments at 15; America On-Line Comments at 7-9; CIEA Reply at 3-5.

700 Internet Access Coalition Reply at 7-8.

701 *Id.*

702 *See, e.g.,* USTA Comments at 81-82; GVNW Comments at 15; GCI Comments at 9.

technologies.[703] GCI claims that usage charges set at the proper level should encourage an economically appropriate level of usage and should help alleviate network congestion caused by users who remain on-line for long periods of time.

200. ISPs and consumer groups insist that accounts of network congestion are greatly exaggerated by the LECs.[704] Internet Access Coalition states that the studies presented by the Bell Operating Companies (BOCs) were based on isolated, worst-case situations, and therefore, the studies fail to give an accurate picture of the impact of data traffic on the BOC networks.[705] Commenters claim that the switch problems which occur in a small number of central offices can be resolved with the technologically simple solutions that the incumbent LECs routinely use when end-users other than ISPs create similar congestion anomalies.[706] PSINet asserts that the BOCs were in a position to anticipate increased network traffic because of an increase in the demand for (1) second lines and other services by consumers and (2) business lines by ISPs.[707] PSINet contends that ILECs have been selling excess capacity for several years, and they should have been reinvesting in their networks, making them more responsive to their Internet customers and better able to handle increase in Internet traffic.[708]

201. *Incentive to switch to packet-switched network.* Some LECs contend that without usage charges for the lines connecting the ISPs to their customers, ISPs have little incentive to use services and technologies that lessen the load on the traffic-sensitive portion of the current switched network or to divert Internet traffic from the circuit-switched local network to more efficient packet-switched networks.[709] ACTA states that radically reformed, rational, cost-based access charges borne by ISPs and other users of the telecommunications infrastructure will provide incentives to improve and optimize today's telecommunications infrastructure and stimulate investment which will assure an adequate supply of capacity and

---

[703] USTA Comment at 82.

[704] *See, e.g.*, Consumer Project Comments at 1; America On-Line Comments at 13-14; CompuServe/Prodigy Comments at 14; Internet Access Coalition Comments at 13; PSINet Comments at 8.

[705] Internet Access Coalition Comments at 13.

[706] *Id.* at 14; *see also* America On-Line Reply at 10.

[707] PSINet Reply at 7-8; *see also,* America On-Line Reply at 12.

[708] PSINet Reply at 7-8.

[709] *See, e.g.*, BA/NYNEX Comments at Attachment 1: Crandall Affidavit at 14-15; PacTel Reply at Attachment 1, Parker Affidavit at 6.

services.[710] SONETECH states that it is natural for ISPs to be CLECs and IXCs, and that access charges would act as an incentive for ISPs to move in that direction.[711]

202. America On-Line urges the Commission to reject LEC statements which suggest that ISPs have incentives to use inefficient services and facilities that will persist as long as the Commission refrains from imposing its access charge rules.[712] America On-Line and Internet Access Coalition state that ISPs know that their customers want higher speed access to the Internet and other on-line services and to the extent that incumbent LECs, or any other entity, offer an efficient, reliable and economic means to provide ISPs' product to the consumer, ISPs have every incentive to use it to the ultimate benefit of the public.[713] America On-Line states that the ISP market is extremely competitive and every provider has powerful market incentives to offer the most reliable, cost-effective, efficient and quality service it can.[714]

203. CPT claims that usage-based charges on basic voice service and ISDN calls from residential users, and usage-based charges for the unbundled loop undermine the LECs' incentives to deploy technologies that solve congestion problems. Collecting usage fees through the circuit switched netowrk then becomes highly profitable and technologies which eliminate the rationale for those charges would threaten this profit center.[715] CPT proposes that the Commission should leave the pricing of basic voice services as is, and require LECs to eliminate the usage charges on higher bandwidth residential digital services like ISDN, if the call is terminated using the new packet switched service.[716]

204. *Discrimination.* PacTel argues that by not requiring ISPs to pay access charges. the Commission discriminatorily grants a preference in rates to ISPs.[717] PacTel states that ISPs are not like regular business customers, that they are more like IXCs because of the way

[710] ACTA Comments at 27.

[711] SONETECH Comments at 3-4.

[712] America On-Line Reply at 13-15.

[713] *Id.*; Internet Access Coalition Reply at 11.

[714] America On-Line Reply at 13-15.

[715] Consumer Project Reply at 6.

[716] *Id.*

[717] PacTel Comments at 74-75.

their customers connect with them.[718]

205. CIEA claims that the mere difference in the payment mechanisms for ISPs and IXCs does not show discrimination in favor of ISPs. CIEA explains that IXCs use different aspects of the local exchange network that ISPs and their Internet customers do not use. For example, outdialing, 911 service, and directory assistance services are used by IXCs, but are not required by ISPs. CIEA states that IXCs have more rights and privileges in interconnecting with the local exchange than ISPs do. Furthermore, states CIEA, IXCs and ISPs pay LECs in different ways because all users of the PSTN pay in different ways, based on their pattern of use.[719]

206. America On-Line contends that requiring ISPs to pay access charges would constitute discrimination because other end-users are not required to pay access charges. Internet Access Coalition agrees, stating that treating ISPs like other end-users is not discriminatory since ISPs are end-users. Internet Access Coalition states that ISPs use business lines solely to receive incoming calls, and, thus, they don't pay originating call fees, just like numerous other business customers -- such as call centers, mail order providers, radio talk shows, and many financial institutions.[720]

207. *Anti-competitive acts by LECs.* Several commenters have expressed a concern that assessing access charges on ISPs will lead LECs to engage in anti-competitive activities.[721] Compuserve and Prodigy state that RBOCs function not only as the dominant providers of access upon which the independent ISPS are dependent to reach their customers, but are also competitors to the independent ISPs in providing information services.[722] CompuServe\Prodigy contend that any access charges collected by the parent RBOC from its affiliated ISP merely represents an intra-corporate transfer among RBOC affiliates with no real overall economic effect to the RBOC or its affiliate. Independent ISPs, however, would have to absorb any increase in access charges to stay in business.[723]

208. PacTel counters that the Commission has extensive rules ensuring that the largest

---

[718] PacTel Reply at 27.

[719] CIEA Reply at 6-8.

[720] Internet Access Coalition Reply at 10-11.

[721] Consumer Project Reply at 3; CIEA Comments at 8; CompuServe/Prodigy Comments at 15; Internet Access Coalition Comments at 19-20; PSINet at 9-10; SONETECH at 4.

[722] CompuServe\Prodigy Comments at 15.

[723] *Id.*

LECs, the BOCs, provide interconnection to third-party ISPs that is comparable, including identical prices, to the interconnection that they provide to their own enhanced service operations. Furthermore, states PacTel, the Commission has extensive accounting rules and other safeguards to ensure against LEC cross-subsidies to support their enhanced services operations.[724]

C. Terminating Access

1. Incumbent LECs

209. Several IXCs and other commenters supported limiting terminating access rates to forward-looking economic cost. Those advocating that the Commission hold terminating access rates to TSLRIC levels cite the absence of competitive pressures on the terminating access provider. They contend that even as originating access services become more competitive, price cap LECs will retain the ability to exercise market power over terminating access, justifying a prescriptive approach that would limit terminating access rates to forward-looking cost.[725] They also emphasize the likelihood of continued ILEC dominance in the provision of access services in the foreseeable future.[726] A number of commenters support the development of TSLRIC studies as a basis for establishing cost-based rates for terminating access.[727]

210. According to incumbent LECs and other commenters, however, sufficient competitive forces exist to constrain the prices charged for terminating interstate access service. For example, USTA challenges the fundamental premise that, because the called party is not paying for the call, terminating access charges are shielded from downward market pressures. Thus, according to these commenters, if a LEC overprices terminating access relative to originating access, a pair of callers in repeated communications would have an incentive to alter their pattern of calls to favor the lower-priced alternative.[728] Other commenters argue that the availability of unbundled network elements and interconnection arrangements will act as a constraint on potentially excessive terminating access charges as

---

[724] PacTel Reply at Parker Affidavit p. 5.

[725] CompTel Comments at 19; Cable & Wireless Comments at 31; ACTA Comments at 23; LCI Comments at 3; TCI Comments at 36; Allied Communications Comments at 3; WorldCom Comments at 92.

[726] AT&T Comments Appendix A at 18; LCI Comments at 3; Cable & Wireless Comments at 31.

[727] *See, e.g.,*TRA Comments at 38-39; California Commission Comments at 17; LCI Reply at 6-7.

[728] USTA Comments Attachment 3 at 12; TCI Comments, Attachment A at 4.

alternative access providers offer competitive services.[729] High terminating rates, these commenters argue, will encourage IXCs to purchase unbundled network elements to complete long-distance calls themselves.[730]

2. Non-Incumbent LECs

211. Competitive LECs urge the Commission to refrain from imposing any direct regulation of their terminating access charges. They contend that competitive LECs lack the kind of market power that would enable them to charge IXCs excessive terminating access rates.[731] Competitive LEC negotiations with IXCs, they explain, have resulted in terminating access charges equal to or below the terminating access rates contained in incumbent LEC tariffs.[732] Commenters assert that IXCs are sophisticated customers with bargaining leverage over competitive LECs and will take necessary actions to discourage excessive charges for terminating access.[733] Other commenters argue that competitive LECs, like incumbent LECs, will restrain their terminating access charges to lower the incentive for IXCs to purchase unbundled network elements to provide their own local access.[734] Spectranet argues that initial dependence of competitive LECs on large volume customers will discourage unreasonable terminating access rates because high rates would entice IXCs to substitute terminating special access for these users.[735] Competitive LECs also express the concern that strict regulation of their terminating access rates would impose an additional burden on their ability to enter the market and compete successfully.[736]

212. Other commenters favor regulation of the terminating access rates of competitive LECs, suggesting that bottleneck control of the called party's loop necessitates some level of

[729] USTA Comments at 67; Ameritech Comments at 53; BA/NYNEX Comments at 42.

[730] USTA Comments at 67; Ameritech Comments at 52-53; BA/NYNEX Comments at 42; SNET Comments at 54; BellSouth Reply at 40; SWBT Reply at 46-47.

[731] ALTS Comments at 29; American Communications Services Reply at 21.

[732] TCI Comments, Attachment A at 6 (*citing* Comments of Spectranet International, Inc., CC Docket No. 92-262 at 7).

[733] Spectranet Comments at 7-8; ICG Telecom Group Reply at 23.

[734] ACC Long Distance Reply at 10; Cox Communications Reply at 4-5; Spectranet Comments at 7-8.

[735] Spectranet Comments at 8.

[736] Time Warner Comments at 49-50; WinStar Comments at 5-6.

regulation.[737] Although incumbent LECs argue that regulation of terminating access is unnecessary, they contend that any regulation of incumbent LEC terminating access should entail equivalent regulatory treatment of competitive LECs because they hold the same degree of market power with respect to the loops they control.[738]

D. Universal Service-Related Part 69 Changes

213. Many parties note that the Commission must carefully coordinate access charge reform and universal service reform.[739] Commenters agree generally that, in order to prevent double recovery and remove implicit subsidies, access charges must reflect receipt of universal service support above current levels.[740] Other parties argue, however, that double recovery is unlikely, especially for rural carriers for whom revenues will be insufficient to maintain service in high cost areas, even if access charges remain unchanged.[741] Several non-price cap incumbent LECs argue that it is premature to address the issue of potential double recovery, particularly for small, rural, rate-of-return LECs, until the details of the universal service fund mechanism are established and the Commission has assessed the cumulative impact of the universal service, access reform, and separations proceedings.[742]

214. The Alabama and Texas Commissions express concern that reducing interstate access rates to reflect universal service revenues will divert funds traditionally used to support intrastate high costs to offset interstate rates, which may only be accomplished by a

[737] AT&T Comments at 63; WorldCom Comments at 92; Ohio Commission Comments at 12.

[738] USTA Comments at 67; BA/NYNEX Comments at 42; BellSouth Comments at 86; PacTel Comments at 74; Rural Telco Coalition Comments at 23-24.

[739] *See, e.g.*, Arch Communications Reply at 1; Alaska Telephone Association Comments at 7; TDS Comments at 27, Reply at 7; Texas Commission Comments at 30; Washington Commission Comments at 9.

[740] *See, e.g.*, Arch Communications Reply at 1; AT&T Comments at 65; Cable & Wireless Comments at 28, n.33 (asserting that the portion of current rates that is universal service subsidy must be separated from rates to comply with the *Universal Service* proceeding); California Commission Comments at 13-14; Internet Access Coalition Comments at 6; PacTel Comments at 50; PCIA Comments at 3-4, Reply at 2-3; Sprint Comments at 54; TCI Reply at 28-29.

[741] *See, e.g.*, Alaska Telephone Association Comments at 7; Western Alliance Comments at 19-20.

[742] *See, e.g.*, Evans, *et al.* Comments at 3; Puerto Rico Tel. Comments at 20-21; TCA Comments at 4-5; TDS Comments at 26, 28, Reply at 7; Western Alliance Comments at 19-20; *see also* American Communications Services, Inc. Reply at 8-9 (asserting that Commission should defer access reform until universal service and separations reform are adopted).

recommendation of a Federal-State Joint Board.[743] These Commissions conclude that a separate component is necessary within the universal service fund that will replace the explicit subsidy reflected in the common line elements of interstate access.[744] The Ohio Commission notes that any downward adjustment of interstate access rates must be based only on the interstate revenues received through the universal service fund mechanism.[745]

215. BA/NYNEX contend that, to the extent universal service payments are intended to cover shortfalls in intrastate payments, a downward adjustment of interstate access rates would in effect be double-counting and would take away the revenue support that the LEC had just received from the universal service fund.[746] Thus, any adjustment to access charges must reflect only the portion of universal service support that covers shortfalls in interstate cost recovery.[747]

216. Several commenters contend that universal service funds should not be used to reduce interstate costs recovered through access charges.[748] These parties argue that neither universal service fund subsidies that keep local exchange rates below cost nor "support funds" that compensate carriers for the discounted portion of the rates for telecommunications services provided to schools, libraries, and rural health care providers, may be used to reduce costs recovered through interstate access charges.[749] Thus, a universal service support payment should not result in a *per se* decrease in interstate access charges unless it is specifically identified as replacing identified means of cost recovery that had previously been

---

[743] Alabama Commission Comments at 14; Texas Commission Comments at 30.

[744] Alabama Commission Comments at 14 (proposing separate components for both high-cost assistance for intrastate services and interstate common cost recovery); Texas Commission Comments at 30-31.

[745] Ohio Commission Comments at 11 (assertign that, if intrastate revenues are used to assess contributions and used to distribute assistance to recipients of universal service support, incumbent LECs that are net beneficiaries of support should be permitted to make downward adjustments to intrastate costs).

[746] BA/NYNEX Comments at 61.

[747] BA/NYNEX Comments at 61.

[748] *See, e.g.*, Ameritech Reply at 34 (opposing attempt to require the recipient carrier to use universal service funds for reducing access charges); Western Alliance Comments at 20; WITA Comments at 9; *see also* State Consumer Advocates Reply at 15 (arguing that TIC, interstate transport and interstate switched access are not services that the Joint Board has designated for universal service support); *but see* BA/NYNEX Reply at 6-7 (arguing that certain funds that LECs receive from the new universal service fund may be used to offset current revenues from interstate access services).

[749] *See, e.g.*, Ameritech Reply at 34.

afforded by access charges.[750] ALLTEL asserts that, because the LTS and DEM weighting mechanisms are the only components of the proposed universal service plan that have direct relationship to access, other universal service support components are designed to offset cost of providing local service in high cost areas and, as such, do not require a corresponding reduction in access rates.[751]

217. According to the Washington Commission, a possible approach to preventing double recovery is to adopt a presumption that any revenues obtained from the universal service fund would be offset against recovery claimed from access charges, and incumbent LECs would bear the burden of establishing to the regulatory authority that additional recovery was appropriate.[752] NARUC asserts that incumbent LECs should have the burden of demonstrating that double recovery will not occur through the combination of restructured access charges and universal service support.[753] TCI argues that incumbent LECs should not be permitted to adjust their price cap indices upwards to permit recovery of their contributions payments unless, at a minimum, they can show that they are actually funded by interstate switched access charges.[754]

218. Several incumbent LECs argue that, to the extent that LECs will have to contribute to any new universal service support mechanism, access charge reduction that would occur as a result of receiving universal service support above current levels must be offset by the amount the LEC has to contribute to the universal service fund.[755] According to PacTel, any exogenous downward adjustment to price cap indices is appropriate to reflect any additional revenues received from the new universal service fund, provided the adjustment is made only to the extent that there is a net revenue increase to the LEC, and the decrease is offset with an exogenous upward adjustment to reflect the extent to which the LEC is unable to pass its own contributions through to its customers.[756] BellSouth contends that unless the Commission establishes a surcharge recovery mechanism to recover LEC contributions to the

---

[750] *See, e.g.*, Puerto Rico Tel. Comments at 19; TDS Reply at 7 (arguing that any off-set for interstate access revenues to prevent double recovery must match support from the new mechanism that it is designed to replace).

[751] ALLTEL Comments at 14.

[752] Washington Commission Comments at 9.

[753] NARUC Comments at 8; *but see* TDS Comments at 28 (no reason to presume federal universal service support causes over-recovery unless it is subtracted from whatever interstate cost allocations are then in effect).

[754] TCI Reply at 30.

[755] *See, e.g.*, BA/NYNEX Comments at 61; BellSouth Comments at 53, n.99; PacTel Comments at 49.

[756] PacTel Comments at 49.

new universal service fund, then LECs must recover their contributions through an access charge mechanism, such as a per line charge assessed to IXCs.[757]

219. Many of the parties commenting on the issue support the Commission's proposal to account for the receipt of explicit universal service revenues, including LTS, through an exogenous cost adjustment to the price cap indices of incumbent LECs.[758] TCI argues that incumbent LECs will double recover if price caps are not adjusted to recognize the elimination of LTS support obligations.[759] Many incumbent LECs, however, agree that the Commission must remove LTS payments from access charges and recommend that these costs be removed from the CCL charge to comply with the 1996 Act requirement that universal service support payments be explicit.[760]

220. Many commenters further propose that price cap LECs should be required to offset access charges by the amount of any increase in universal support payments above current universal service funding, and apply this reduction to the CCL or any new mechanism that replaces it.[761] Other commenters offer more specific proposals for applying adjustments to particular baskets or service categories in a particular order. For example, BellSouth recommends that universal service funds first be applied to reducing the CCL charge, then to the TIC service category in the trunking basket, and finally to the local switching service category in the traffic sensitive basket.[762] Alternatively, Sprint suggests that, if the Commission adopts Sprint's proposal to access reform by eliminating the CCL charge and reducing access rates to TELRIC-based prices, the required reductions in the price cap index be applied first to the TIC and then to the difference between current rates and TELRIC-based rates for traffic sensitive switching and transport. If the Commission does not eliminate the

[757] BellSouth Reply at 7, n.11

[758] *See, e.g.*, ACTA Comments at 22; California Commission Comments at 13-14; Internet Access Coalition Comments at 6; Sprint Comments at 54; Texas Commission Comments at 30; TCI Comments at 34, Reply at 29.

[759] TCI Reply at 29-30; *see also* ALLTEL Comments at 14 (arguing that once LTS and DEM weighting and transitioned to the high cost universal service fund, there should be a corresponding dollar-for-dollar reduction in associated access rates).

[760] *See, e.g.*, U S West Comments at 53; *see also* Ameritech Comments at 50-51, Reply at 34; BellSouth Comments at 68.

[761] *See, e.g.*, ACTA Comments at 22 (arguing that CCL charges should be reduced to the extent that recovery of LTS from other sources is not offset by a SLC cap reduction); California Commission Comments at 13-14 (asserting that CCL charges should be reduced to the extent universal service funding is directed to support high-cost loops); SWBT Comments at 6 (maintaining that CCL charges should be reduced by the amount of high cost support incumbent LECs receive from the new universal service fund).

[762] BellSouth Comments at 53-54.

CCL charge, however, Sprint proposes that incumbent LECs should be required to apply their incremental universal service revenues against the price cap indices for both the CCL charge and TIC in equal proportions until both elements are eliminated, and then against rates for traffic-sensitive local switching and transport.[763]

221. Several non-price cap LEC parties assert that there is no need to adjust interstate costs for rate-of-return ILECs to reflect universal service revenues because double recovery is unlikely.[764] For example, WITA asserts that there is no double recovery if the receipt of funds is based on a benchmark that is calculated on a national average revenue per line, including revenue generated from access services because it is only the cost of local service in excess of the benchmark that is funded through the USF mechanism.[765] Evans, *et al.* notes that, because the present system limits universal service payments to loop costs not included under the interstate gross allocator and makes the offsetting cost reduction to intrastate costs, any new universal service fund system should continue to offset intrastate costs.[766] The Minnesota Independent Coalition contends that either local service rates or universal service revenues must necessarily increase if access charges paid by IXCs decrease.[767]

222. Several parties commented on the way in which non-price cap LECs' interstate access charges should be adjusted to account for removal of implicit LTS subsidies and any increase in explicit universal service support revenues. Most commenters favoring a downward exogenous cost adjustment for price cap LECs' price cap indices also support a similar downward adjustment to non-price cap LECs' access rates.[768] USTA and several other non-price cap LECs assert that rate-of-return companies should be permitted to use funding from any new universal service support mechanisms to offset existing explicit universal

[763] Sprint Comments at 54-55.

[764] *See, e.g.*, Alaska Telephone Association Comments at 7; Western Alliance Comments at 20.

[765] WITA Comments at 9; *see also* Cathey, Hutton and Associates Comments at 4 (asserting that recovery will not be "double" but will only alter the amount of costs recovered from access rates versus the amount of costs recovered from the new universal service fund mechanism because access rates will be calculated into the benchmark revenues to be used to offset proxy-based universal service costs); Western Alliance Comments at 21 (arguing that, because the proxy models in *Universal Service* proceeding have deleted DEM weighting and LTS, there is no need to subtract the universal service support payments paid to rural LECs from the interstate costs used to develop rural LECs' access charges).

[766] Evans, *et al.* Comments at 3.

[767] Minnesota Independent Coalition Comments at 18.

[768] *See, e.g.*, PCIA Comments at 3-4; Sprint Comments at 54, n.23.

service requirements before reducing any Part 69 rates.[769] USTA argues that Part 69 rate reductions, *i.e.*, decreases in the level of this implicit support mechanism, should only take place to the extent that new universal service revenues exceed existing explicit universal service requirements.[770] Roseville Tel. supports allowing non-price cap LECs to continue to use universal service revenues to offset intrastate revenue shortfalls and, for any universal service support greater than the amount currently received (including LTS), use that to reduce the CCL charge and then the SLC.[771] Should the Commission reduce interstate costs to reflect revenues received from any new universal service support mechanism to the extent allocated to the interstate jurisdiction, however, Roseville Tel. cautions that intrastate rates will have to be raised to address the shortfall that is currently covered by universal service support.[772]

223. According to NECA, the Commission should clarify that, absent changes in the separations rules, interstate revenue requirements would continue to be determined as they are today.[773] NECA further advocates that the Commission adopt Part 69 rule changes that treat new universal service amounts allocated to the interstate access elements, including DEM weighting and LTS, as revenue streams in the development of interstate access rates.[774] NECA proposes that revenues from the new universal service fund be used to offset the pool common line revenue requirement, in a manner similar to the way the SLC offsets CCL rates.[775] In developing its traffic-sensitive local switching rates, NECA would consider all revenue projected for its common line pooling members, as well as any proxy-based amounts for pooling companies that are allocated to interstate common line.[776] In addition, NECA argues that the Commission should clarify that the per-line rural transition high-cost support amounts from the new universal service fund should continue to be treated as an intrastate expense adjustment recovered from the interstate jurisdiction to help keep intrastate rates

[769] *See, e.g.*, GVNW Comments at 12; Puerto Rico Tel. Reply at 8; TDS Comments at 27; USTA Comments at 69.

[770] *See, e.g.*, Puerto Rico Tel. Reply at 8; USTA Comments at 69.

[771] Roseville Tel. Comments at 16.

[772] Roseville Tel. Comments at 16.

[773] NECA Comments at 14.

[774] NECA Comments at 14-15.

[775] NECA Comments at 15.

[776] NECA Comments at 15; *see also* TDS Comments at 27 (arguing that LTS should continue to be treated as an interstate revenue stream for the NECA Common Line pool).

affordable.[777] NECA notes that this may require Part 36 rule changes to ensure matching of the expense adjustment with the level of federal universal service funding ultimately adopted.[778]

E. Part 69 Allocation Rules

224. In the NPRM, we solicited comment on whether it would be appropriate for incumbent price cap LECs to be relieved of complying with Subparts D and E of Part 69 of our rules, which address the allocation of investments and expenses to the access rate elements.[779]

225. Many of the commenters recommend that the Commission eliminate Subparts D and E.[780] GTE argues that the allocation rules are outdated and unnecessarily inhibit the introduction of new services and technologies, thereby limiting incumbent LECs' ability to respond to competition.[781] GTE argues that the cost allocation rules, which are predicated on rate base regulation, serve no purpose in GTE's proposed access regime, which includes a simplification of price baskets and an elimination of sharing requirements and low end adjustments.[782] BellSouth contends that it does not use the cost allocation rules for ratemaking, and instead uses them only for internal purposes.[783] BellSouth acknowledges that the cost allocations rules are necessary to complete the ARMIS reports, but contends that with a market-based approach to access reform, neither the ARMIS reports nor the cost allocation rules are necessary.[784]

226. TCI recommends that, commensurate with its suggested hybrid

---

[777] NECA Comments at 15; *see also* Evans, *et al.* Comments at 3 (asserting that any new universal service support system should continue to offset intrastate costs).

[778] NECA Comments at 15, n.46.

[779] NPRM at ¶ 294.

[780] Ameritech Comments at 56; BA/NYNEX Comments at 60; BellSouth Comments at 88; GTE Comments at 46-47.

[781] GTE Comments at 46-47. *See also* BA/NYNEX Comments at 60 (elimination of sharing mechanism under market-based approach will allow Commission to eliminate onerous cost allocation rules).

[782] GTE Comments at 47.

[783] BellSouth Comments at 88 (although BellSouth uses cost allocation rules to develop exogenous cost data internally, this data can be calculated in other ways).

[784] BellSouth Comments at 88.

market/prescriptive approach to access reform, the Commission should retain the cost allocation rules until there is substantial competition on a service-by-service basis in a defined geographic market. TCI urges the Commission to proceed cautiously in lifting this type of regulation, contending that premature regulatory flexibility could have anticompetitive consequences due to the incumbent LECs' existing market power.[785] The Georgia Commission contends that the Commission should verify and analyze costs prior to moving to a transitional phase of market-based or prescriptive approach. If the Part 69 rules aid in that process, the Georgia Commission argues that they should be retained.[786]

F. Other Proposed Part 69 Changes

227. The commenters generally agree with the majority of our specific proposals concerning Part 69 revisions.[787] Sprint contends that the NPRM's proposed revisions are non-controversial and should be adopted.[788] Ameritech favors incorporating the previously-granted waivers into Part 69.[789]

228. Some commenters expressed dissatisfaction with various parts of our Part 69 proposals. For example, BellSouth objects to the proposal that "Telephone Company" be defined as "incumbent LEC" as set out in section 252(h)(1) of the 1996 Act because it believes that Part 69 should apply to all LECs, not just incumbent LECs. BellSouth argues that until forbearance determinations are made, all LECs remain subject to the Part 69 rules.[790] BellSouth also opposes the proposal to codify the various Part 69 waivers previously granted, arguing that the waiver orders are sufficiently explanatory, the alternative rate structures are too cumbersome to describe, and the end result would be more, rather than less, regulation.[791]

229. GCI suggests modifications to our proposal to eliminate those sections connected to the equal access rate element. GCI contends that some LECs have not fully recovered equal access costs. GCI also notes that in some areas, such as the Alaska bush, where

---

[785] TCI Comments at 40. *See also* TCI Reply at 26.

[786] Georgia Commission Reply at 43

[787] *See, e.g.,* Ameritech Comments at 56; BellSouth Comments at 88-90; Sprint Comments at 60; WorldCom comments at 94 (supporting Commission's proposal that clarifies that Part 69 access charge rules apply to incumbent LECs and not to CLECs).

[788] Sprint Comments at 60.

[789] Ameritech Comments at 56.

[790] BellSouth Comments at 89.

[791] BellSouth Comments at 90.

facilities-based interexchange competition has been prohibited, many LECs have not yet implement equal access. To account for these concerns, GCI recommends that section 69.107, which allows carriers to establish a separate equal access rate element, be eliminated. GCI contends that sections 69.308 and 69.410 should be modified to provide that the costs be assigned to the Local Switching element. GCI also recommends that we retain both the reference to section 69.308 found in section 69.309, and the reference to section 69.410 found in section 69.411. GCI contends that recovery through the Local Switching element is preferable to the general allocation that would otherwise be applicable.[792]

230. Ameritech suggests that Part 69 be changed to permit LECs the flexibility to introduce new switched access rate elements without the current barriers.[793] TCA and NECA recommend that rate-of-return LECs be allowed to introduce new services though the expedited process established for incumbent LECs in the Third Report and Order.[794]

231. In response to our request for additional revisions, many commenters suggested that the Part 69 rules be completely eliminated.[795] Many of the LECs argue that Part 69 rules are unnecessarily restrictive, inhibiting the LECs' abilities to respond to competition, impairing their ability to introduce new services, or failing to account for changes in technology.[796] USTA recommends as part of the market-based Phase I approach, the Commission should replace the current Part 69 rules with streamlined rules that would address the recovery of the CCL, TIC, and depreciation reserve deficiency without codifying specific rate elements.[797] USTA also recommends that Part 69 should be retained for rate-of-return

[792] GCI Comments at 8. *See also* TCA Comments at 5-6 (equal access rate elements should not be removed because some small LECs who have not received a bona fide request to convert should be allowed same treatment of their equal access costs as other LECs).

[793] Ameritech Comments at 42, 56.

[794] TCA Comments at 6; NECA Comments at 14 (referencing Access Reform Third Report and Order, ¶¶ 309-310).

[795] USTA Comments at 48; Ameritech Comments at 56; BA/NYNEX Comments at 60; BellSouth Comments at 88; GTE Comments at 46-47; NECA Reply at 10; SNET Reply at 14.

[796] GTE Comments at 47; SNET Comments at 19-20; SNET Reply at 14; Internet Access Coalition Comments at 5; NECA Reply at 10; NARUC Comments at 5.

[797] USTA Comments at 48. *See also* USTA Reply at 26 (simplification of price baskets and elimination of Part 69 rules will enhance LECs' economic efficiency).

companies, but modified in a separate proceeding to reflect the recovery of the CCL and TIC.[798] NECA argues that Part 69 rules needlessly increase administrative expense.[799]

[798] USTA Comments at 48.

[799] NECA Reply at 10 (elimination or simplification of rules is sound administrative practice irrespective of level of competition).

APPENDIX C - Final Rules

AMENDMENTS TO THE CODE OF FEDERAL REGULATIONS

PART 61 -- TARIFFS

1. The authority citation for Part 61 continues to read as follows:

Authority: Secs. 1, 4(i), 4(j), 201-205, and 403 of the Communications Act of 1934, as amended; 47 U.S.C. 151, 154(i), 154(j), 201-205, and 403, unless otherwise noted.

2. Section 61.3 is amended by revising the introductory text of paragraph (f) to read as follows:

§ 61.3 Definitions

* * * * *

(f) **Basket.** Any class or category of tariffed service or charge:

* * * * *

[3]. Section 61.42 is amended by revising [paragraphs] (d)(1), (d)(2), and (d)(3), adding paragraph (d)(6), and revising paragraphs (e)(1) and (e)(2)(vi) to read as follows:

§ 61.42 Price cap baskets and service categories.

* * * * *

(d) * * *

(1) A basket for the common line interstate access elements as described in §§ 69.115, 69.152, 69.154, and 69.157 of this chapter, and that portion of the interstate access element described in § 69.153 of this chapter that recovers common line interstate access revenues;

(2) A basket for traffic sensitive switched interstate access elements;

(3) A basket for trunking services as described in §§ 69.110, 69.111, 69.112, 69.114, 69.125(b), and 69.155 of this chapter, and that portion of the interstate access

element described in § 69.153 of this chapter that recovers residual interconnection charge revenues;

* * * * *

(6) A basket for the marketing expenses described in § 69.156 of this chapter, including those recovered through End User Common Line charges and Presubscribed Interexchange Carrier charges.

(e)(1) The traffic sensitive switched interstate access basket shall contain such services as the Commission shall permit or require, including the following service categories:

(i) Local switching as described in § 69.106(f) of this chapter;

(ii) Information, as described in § 69.109 of this chapter;

(iii) Data base access services;

(iv) Billing name and address, as described in § 69.128 of this chapter;

(v) Local switching trunk ports, as described in § 69.106(f)(1) of this chapter; and

(vi) Signalling transfer point port termination, as described in § 69.125(c) of this chapter.

(2) * * *

(vi) Interconnection charge, as recovered in §§ 69.153 and 69.155 of this chapter.

* * * * *

4. Section 61.45 is amended by revising the introductory text of paragraph (b) and (b)(1), redesignating the introductory text of paragraph (c) as the introductory text of paragraph (c)(1) and revising it, and adding new paragraphs (c)(2), (d)(1)(ix), (i), (j), (k), and (l) to read as follows:

§ 61.45 Adjustments to the PCI for Local Exchange Carriers.

* * * * *

(b) Adjustments to local exchange carrier PCIs for the baskets designated in § 61.42(d)(2), (3), (4), (5), and (6) shall be made pursuant to the formula set forth in § 61.44(b), and as further explained in §§ 61.44(e), (f), (g), and (h).

(1) Notwithstanding the value of X defined in § 61.44(b), the X value applicable to the baskets specified in § 61.42(d)(2), (3), and (6) shall be 4.0%, or 4.7%, or 5.3%, as the carrier elects.

* * * * *

(c)(1) Subject to paragraphs (c)(2) and (e) of this section, adjustments to local exchange carrier PCIs for the basket designated in § 61.42(d)(1) shall be made pursuant to the following formula:

* * * * *

(2) The formula set forth in paragraph (c)(1) of this section shall be used by a local exchange carrier subject to price cap regulation only if that carrier is imposing a carrier common line charge pursuant to § 69.154 of this chapter. Otherwise, adjustments to local exchange carrier PCIs for the basket designated in § 61.42(d)(1) shall be made pursuant to the formula set forth in § 61.44(b), and paragraphs (i) and (j) of this section, and as further explained in § 61.44(e), (f), (g), and (h). For the purposes of this paragraph, and notwithstanding the value of X defined in § 61.44(b), the X value applicable to the basket specified in § 61.42(d)(1) shall be 4.0%, or 4.7%, or 5.3%, as the carrier elects.

(d) * * *

(1) * * *

(ix) The completion of amortization of equal access expenses.

* * * * *

(i)(1) Notwithstanding the provisions of paragraphs (b) and (c) of this section, and subject to the limitations of paragraph (j) of this section, price cap local exchange carriers that are recovering interconnection charge revenues through per-minute rates pursuant to § 69.124 or § 69.155 of this chapter shall target, to the extent necessary to eliminate the recovery of any residual interconnection charge revenues through per-minute rates, any PCI reductions associated with the baskets designated in § 61.42(d)(1) and (2) that result from the application of the formula in § 61.45(c) and, pursuant to § 61.45(b), application of the formula in § 61.44(b), as further explained in § 61.44(e), (f), (g), and (h), to the PCI for the basket designated in § 61.42(d)(3), with no adjustment being made to the PCIs for the baskets designated in § 61.42(d)(1) and (2) as a result of the application of the formulas in § 61.44(b) and § 61.45(c). These reductions are to be made after the adjustment is made to the PCI for the basket designated in § 61.42(d)(3) resulting from the application of the formula in § 61.44(b), as further explained in § 61.44(e), (f), (g), and (h).

(2) Notwithstanding the provisions of paragraph (b) of this section, and subject to the limitations of paragraph (j) of this section, price cap local exchange carriers that are recovering interconnection charge revenues through per-minute rates pursuant to § 69.155 of this chapter shall target, to the extent necessary to eliminate the recovery of any residual interconnection charge revenues through per-minute rates, any PCI reductions associated with the basket designated in § 61.42(d)(6) that result from the application, pursuant to § 61.45(b), of the formula in § 61.44(b), as further explained in § 61.44(e), (f), (g), and (h), to the PCI for the basket designated in § 61.42(d)(3), with no adjustment being made to the PCIs for the basket designated in § 61.42(d)(6) as a result of the application of the formula in § 61.44(b). This reduction is to be made after any adjustment made pursuant to paragraph (i)(1) of this section.

(3) Through December 31, 1997, the reduction in the PCI for the basket designated in § 61.42(d)(3) that results from paragraph (i)(1) of this section shall be determined by dividing the sum of the dollar effects of the PCI reductions that would have applied to the baskets designated in § 61.42(d)(1) and (d)(2) except for the provisions of paragraph (i)(1) of this section by the dollar amount associated with the PCI for the basket designated in § 61.42(d)(3), and multiplying the PCI for the basket designated in § 61.42(d)(3) by one minus the resulting ratio.

(4) Effective January 1, 1998, the reduction in the PCI for the basket designated in § 61.42(d)(3) that results from paragraphs (i)(1) and (i)(2) of this section shall be determined by dividing the sum of the dollar effects of the PCI reductions that would have applied to the baskets designated in § 61.42(d)(1), (d)(2), and (d)(6), except for the provisions of paragraphs (i)(1) and (i)(2) of this section, by the dollar amount associated with the PCI for the basket designated in § 61.42(d)(3), and multiplying the PCI for the basket designated in § 61.42(d)(3) by one minus the resulting ratio.

(j) In determining the extent of the targeting that shall occur pursuant to paragraphs (i)(1) and (i)(2) of this section and § 61.47(i)(1) and (i)(2), local exchange carriers shall:

(1) compute their anticipated residual interconnection charge amount by excluding revenues that are expected to be reallocated to cost-causative facilities-based charges in the future. To determine interconnection charge amounts so excluded in connection with the July 1, 1997 tariff filings, the local exchange carriers listed below shall use as an estimate of the residual interconnection charge revenues the specified residual interconnection charge percentage: NYNEX, 77.63 percent; BellSouth, 56.93 percent; U S West, 59.14 percent; Bell Atlantic, 63.96 percent; Southwestern Bell Telephone, 69.11 percent; and Pacific Bell and Nevada Bell, 53.52 percent. Each remaining price cap local exchange carrier shall estimate a residual interconnection charge in an amount equal to 55 percent of its current interconnection charge revenues. For subsequent tariff filings in which the PCI reductions are to be targeted to the interconnection charge, these initial estimates shall be adjusted to reflect the actual amounts that have or will be reallocated. If the use of these estimates results in more PCI reductions being targeted to the interconnection charge than required to eliminate the per-minute interconnection charge, the local exchange carrier shall make the necessary exogenous adjustments to reverse the effects of the excess targeting

(2) not include the amounts of any exogenous adjustments reflected in the z component of the formulas in §§ 61.44(b) and 61.45(c). Any such exogenous adjustments shall be reflected in the various PCIs and SBIs in the same manner as they would if there were no targeting.

(k) The calculation of the PCI for the basket designated in § 61.42(d)(3) shall include any residual interconnection charge revenues recovered pursuant to §§ 69.153 and 69.155 of this chapter.

(l) The calculation of the PCI for the basket designated in § 61.42(d)(6) shall include any marketing expense revenues recovered pursuant to §§ 69.153 and 69.156 of this chapter.

5. Section 61.46 is amended by redesignating the introductory text of paragraph (d) as the introductory text of paragraph (d)(1) and revising it, adding new paragraph (d)(2), redesignating paragraph (e) as paragraph (e)(1) and revising it, and adding new paragraphs (e)(2), (g) and (h) to read as follows:

§ 61.46 Adjustments to the API.

* * * * *

(d)(1) Subject to paragraph (d)(2) of this section, and in connection with any price cap tariff proposing changes to rates for services in the basket designated in § 61.42(d)(1), the maximum allowable carrier common line (CCL) charges shall be computed pursuant to the following methodology:

$CCL_{MOU} = CL_{MOU} * (1 + \%\text{ change in CL PCI}) - (EUCL_{MOU} + PICC_{MOU}) * 1 / (1 +(g/2))$

where

CCL_{MOU} = the sum of each of the proposed Carrier Common Line rates multiplied by its corresponding base period Carrier Common Line minutes of use, divided by the sum of all types of base period Carrier Common Line minutes of use,

CL_{MOU} = the sum of each of the existing maximum allowable Carrier Common Line rates multiplied by its corresponding base period Carrier Common Line minutes of use, plus each existing maximum allowable End User Common Line (EUCL) rate multiplied by its corresponding base period lines, plus the common line portion of each existing maximum allowable Presubscribed Interexchange Carrier Charge (PICC) multiplied by its corresponding base period lines, divided by the sum of all types of base period Carrier Common Line minutes of use,

$EUCL_{MOU}$ = maximum allowable End User Common Line rates multiplied by base period lines, and divided by the sum of all types of base period Carrier Common Line minutes of use,

$PICC_{MOU}$ = the common line portion of maximum allowable Presubscribed Interexchange Carrier charge rates multiplied by base period lines, and divided by the sum of all types of base period Carrier Common Line minutes of use, and

g = the ratio of minutes of use per access line during the base period to minutes of use per access line during the previous base period, minus 1.

(2) The formula set forth in paragraph (d)(1) of this section shall be used by a local exchange carrier subject to price cap regulation only if that carrier is imposing a per-minute carrier common line charge pursuant to § 69.154 of this chapter. Otherwise, adjustments to local exchange carrier APIs for the basket designated in § 61.42(d)(1) shall be made pursuant to the formula set forth in paragraph (a) of this section.

(e)(1) In addition, for the purposes of paragraph (d), "Existing Carrier Common Line Rates" shall include existing originating premium, originating non-premium, terminating premium and terminating non-premium rates; and "End User Common Line Rates" used to calculate the CL_{MOU} and the $EUCL_{MOU}$ factors shall include, but not be limited to, Residential and Single Line Business rates, Centrex rates, and the Special Access surcharge.

(2) For purposes of paragraph (d), "each existing Presubscribed Interexchange Carrier Charge" shall include all the charges specified in § 69.153 of this chapter.

* * * * *

(g) The calculation of the API for the basket designated in § 61.42(d)(3) shall include any residual interconnection charge revenues recovered pursuant to §§ 69.153 and 69.155 of this chapter.

(h) The calculation of the API for the basket designated in § 61.42(d)(6) shall include any marketing expense revenues recovered pursuant to §§ 69.153 and 69.156 of this chapter.

6. Section 61.47 is amended by adding paragraphs (g)(7), (i) and (j) to read as follows:

§ 61.47 Adjustments to the SBI; pricing bands.

* * * * *

(g)(1) * * *

(7) The initial level of the local switch trunk ports service category designated in § 61.42(e)(1)(v) shall be established to include those costs identified pursuant to § 69.106(f)(1) of this chapter. This level shall be assigned a value of 100 and, thereafter must be adjusted as provided in paragraph (a) of this section, subject to the banding restrictions of paragraph (e) of this section.

* * * * *

(i)(1) Through December 31, 1997, notwithstanding the requirements of paragraph (a) and subject to the limitations of § 61.45(j), if a local exchange carrier is recovering interconnection charge revenues through per-minute rates pursuant to § 69.124 or § 69.155 of this chapter, any reductions to the PCI for the basket designated in § 61.42(d)(3) resulting from the application of the provisions of § 61.45(b) and the formula in § 61.44(b) and from the application of provisions of § 61.45(i)(1) shall be directed to the SBI of the service category designated in § 61.42(e)(2)(vi).

(2) Effective January 1, 1998, notwithstanding the requirements of paragraph

(a) of this section, and subject to the limitations of §61.45(j), if a local exchange carrier is recovering interconnection charge revenues through per-minute rates pursuant to § 69.155 of this chapter, any reductions to the PCI for the basket designated in § 61.42(d)(3) resulting from the application of the provisions of § 61.45(b), and the formula in § 61.44(b) and from the application of the provisions of § 61.45(i)(1) and (i)(2) shall be directed to the SBI of the service category designated in § 61.42(e)(2)(vi).

(3) Through December 31, 1997, the SBI reduction required by paragraph (i)(1) of this section shall be determined by dividing the sum of the dollar amount of any PCI reduction required by § 61.45(i)(1) by the dollar amount associated with the SBI for the service category designated in § 61.42(e)(2)(vi), and multiplying the SBI for the service category designated in § 61.42(e)(2)(vi) by one minus the resulting ratio.

(4) Effective January 1, 1998, the SBI reduction required by paragraph (i)(2) of this section shall be determined by dividing the sum of the dollar amount of any PCI reduction required by § 61.45(i)(1) and (i)(2), by the dollar amount associated with the SBI for the service category designated in § 61.42(e)(2)(vi), and multiplying the SBI for the service category designated in § 61.42(e)(2)(vi) by one minus the resulting ratio.

(j) The calculation of the SBI for the service category designated in § 61.42(e)(2)(vi) shall include any residual interconnection charge revenues recovered pursuant to §§ 69.153 and 69.155 of this chapter.

7. Section 61.48 is amended by adding paragraph (k) to read as follows:

§ 61.48 Transition rules for price cap formula calculations.

* * * * *

(k) Marketing expenses. In the January 1, 1998 price cap tariff filing, local exchange carriers shall establish the marketing expense basket designated in § 61.42(d)(6) with an initial PCI and API level of 100. The initial value of 100 for the PCI and API for marketing expenses shall correspond to the marketing expenses described in § 69.156(a) of this chapter.

PART 69 -- ACCESS CHARGES

8. The authority citation for part 69 continues to read as follows:

Authority: 47 U.S.C. §§ 154(i) and (j), 201, 202, 203, 205, 218, 254, and 403.

9. Section 69.1(c) is revised to read as follows:

§ 69.1 Application of access charges.

* * * * *

(c) The following provisions of this part shall apply to telephone companies subject to price cap regulation only to the extent that application of such provisions is necessary to develop the nationwide average carrier common line charge, for purposes of reporting pursuant to §§ 43.21 and 43.22 of this chapter, and for computing initial charges for new rate elements: §§ 69.3(f), 69.106(b), 69.106(f), 69.106(g), 69.109(b), 69.110(d), 69.111(c), 69.111(g)(1), 69.111(l), 69.112(d), 69.114(b), 69.114(d), 69.125(b)(2), 69.301 through 69.310, and 69.401 through 69.412. The computation of rates pursuant to these provisions by telephone companies subject to price cap regulation shall be governed by the price cap rules set forth in part 61 of this chapter and other applicable Commission Rules and orders.

10. Section 69.2 is amended by revising paragraph (hh) to read as follows:

§ 69.2 Definitions.

* * * * *

(hh) "Telephone company" or "local exchange carrier" as used in this Part means an incumbent local exchange carrier as defined in section 251(h)(1) of the 1934 Act as amended by the 1996 Act.

* * * * *

11. Section 69.4 is amended by removing paragraphs (b)(1), (d) and (f), revising the introductory text of paragraph (b), and adding paragraph (h) to read as follows:

§ 69.4 Charges to be filed.

* * * * *

(b) Except as provided in § 69.4(c), (e), and (h), and in § 69.118, the carrier's carrier charges for access service filed with this Commission shall include charges for each of the following elements:

* * * * *

(h) In addition to the charges specified in paragraph (b) of this section, the carrier's carrier charges for access service filed with this Commission by price cap local exchange carriers shall include charges for each of the following elements:

(1) Presubscribed interexchange carrier;

(2) Per-minute residual interconnection;

(3) Dedicated local switching trunk port;

(4) Shared local switching trunk port;

(5) Dedicated tandem switching trunk port;

(6) Line port costs in excess of basic, analog service; and

(7) Multiplexers associated with tandem switching.

12. Section 69.103 is removed.

13. Section 69.104 is amended by revising the section heading and paragraphs (a) and (e) to read as follows:

§ 69.104 End user common line for non-price cap incumbent local exchange carriers.

(a) This section is applicable only to incumbent local exchange carriers that are not subject to price cap regulation as that term is defined in § 61.3(x) of this chapter. A charge that is expressed in dollars and cents per line per month shall be assessed upon end users that subscribe to local exchange telephone service or Centrex service to the extent they do not pay carrier common line charges. A charge that is expressed in dollars and cents per line per month shall be assessed upon providers of public telephones. Such charge shall be assessed for each line between the premises of an end user, or public telephone location, and a Class 5 office that is or may be used for local exchange service transmissions.

* * * * *

(e) The monthly charge for each residential and single line business local exchange service subscriber shall be the charge computed in accordance with § 69.104(c), or $3.50, whichever is lower.

* * * * *

14. Section 69.105 is amended by revising the section heading and paragraph (a), and removing paragraphs (b)(7) and (b)(8), to read as follows:

§ 69.105 Carrier common line for non-price cap local exchange carriers.

(a) This section is applicable only to local exchange carriers that are not subject to price cap regulation as that term is defined in § 61.3(x) of this chapter. A charge that is expressed in dollars and cents per line per access minute of use shall be assessed upon all interexchange carriers that use local exchange common line facilities for the provision of interstate or foreign telecommunications services, except that the charge shall not be assessed upon interexchange carriers to the extent they resell MTS or MTS-type services of other common carriers (OCCs).

* * * * *

15. Section 69.106 is amended by revising paragraphs (a) and (b), and by adding paragraphs (f) and (g) to read as follows:

§ 69.106 Local switching.

(a) Except as provided in § 69.118, charges that are expressed in dollars and cents per access minute of use shall be assessed by local exchange carriers that are not subject to price cap regulation upon all interexchange carriers that use local exchange switching facilities for the provision of interstate or foreign services.

(b) The per minute charge described in paragraph (a) of this section shall be computed by dividing the projected annual revenue requirement for the Local Switching element by the projected annual access minutes of use for all interstate or foreign services that use local exchange switching facilities.

* * * * *

(f) Except as provided in § 69.118, price cap local exchange carriers shall establish rate elements for local switching as follows:

(1) Price cap local exchange carriers shall separate from the projected annual

revenues for the Local Switching element those costs projected to be incurred for ports (including cards and DS1/voice-grade multiplexers required to access end offices equipped with analog switches) on the trunk side of the local switch. Price cap local exchange carriers shall further identify costs incurred for dedicated trunk ports separately from costs incurred for shared trunk ports.

(i) Price cap local exchange carriers shall recover dedicated trunk port costs identified pursuant to paragraph (f)(1) of this section through flat-rated charges expressed in dollars and cents per trunk port and assessed upon the purchaser of the dedicated trunk terminating at the port.

(ii) Price cap local exchange carriers shall recover shared trunk port costs identified pursuant to paragraph (f)(1) of this section through charges assessed upon purchasers of shared transport. This charge shall be expressed in dollars and cents per access minute of use. The charge shall be computed by dividing the projected costs of the shared ports by the historical annual access minutes of use calculated for purposes of recovery of common transport costs in § 69.111(c).

(2) Price cap local exchange carriers shall recover the projected annual revenues for the Local Switching element that are not recovered in paragraph (f)(1) of this section through charges that are expressed in dollars and cents per access minute of use and assessed upon all interexchange carriers that use local exchange switching facilities for the provision of interstate or foreign services. The maximum charge shall be computed by dividing the projected remainder of the annual revenues for the Local Switching element by the historical annual access minutes of use for all interstate or foreign services that use local exchange switching facilities.

(g) On or after July 1, 1998, a price cap local exchange carrier may recover signalling costs associated with call setup through a call setup charge imposed upon all interstate interexchange carriers that use that local exchange carrier's facilities to originate or terminate interstate interexchange or foreign services. This charge must be expressed as dollars and cents per call attempt and may be assessed on originating calls handed off to the interexchange carrier's point of presence and on terminating calls received from an interexchange carrier's point of presence, whether or not that call is completed at the called location. Price cap local exchange carriers may not recover through this charge any costs recovered through other rate elements.

16. Section 69.107 is removed.

17. Section 69.111 is amended by removing and reserving paragraphs (b) and (f), revising

paragraphs (a), (c), (d), (e), and (g), and adding paragraph (l) to read as follows:

§ 69.111 Tandem-Switched Transport and Tandem Charge.

(a)(1) Through June 30, 1998, except as provided in paragraph (l) of this section, tandem-switched transport shall consist of two rate elements, a transmission charge and a tandem switching charge.

(2) Beginning July 1, 1998, except as provided in paragraph (l) of this section, tandem-switched transport shall consist of three rate elements as follows:

(i) A per-minute charge for transport of traffic over common transport facilities between the incumbent local exchange carrier's end office and the tandem switching office. This charge shall be expressed in dollars and cents per access minute of use and shall be assessed upon all purchasers of common transport facilities between the local exchange carrier's end office and the tandem switching office.

(ii) A per-minute tandem switching charge. This tandem switching charge shall be set in accordance with paragraph (g) of this section, excluding multiplexer and dedicated port costs recovered in accordance with paragraph (l) of this section, and shall be assessed upon all interexchange carriers and other persons that use incumbent local exchange carrier tandem switching facilities.

(iii) A flat-rated charge for transport of traffic over dedicated transport facilities between the serving wire center and the tandem switching office. This charge shall be assessed as a charge for dedicated transport facilities provisioned between the serving wire center and the tandem switching office in accordance with § 69.112.

(b) [Reserved.]

(c)(1) Through June 30, 1998, tandem-switched transport transmission charges generally shall be presumed reasonable if the telephone company bases the charges on a weighted per-minute equivalent of direct-trunked transport DS1 and DS3 rates that reflects the relative number of DS1 and DS3 circuits used in the tandem to end office links (or a surrogate based on the proportion of copper and fiber facilities in the interoffice network), calculated using the total actual voice-grade minutes of use, geographically averaged on a study-area-wide basis, that the incumbent local exchange carrier experiences based on the prior year's annual use. Tandem-switched transport transmission charges that are not presumed reasonable generally shall be suspended and investigated absent a substantial cause showing by the telephone company.

(2) Beginning July 1, 1998:

(i) Except in study areas where the incumbent local exchange carrier has implemented density pricing zones as described in section 69.124, per-minute common transport charges described in paragraph (a)(2)(i) of this section shall be presumed reasonable if the incumbent local exchange carrier bases the charges on a weighted per-minute equivalent of direct-trunked transport DS1 and DS3 rates that reflects the relative number of DS1 and DS3 circuits used in the tandem to end office links (or a surrogate based on the proportion of copper and fiber facilities in the interoffice network), calculated using the total actual voice-grade minutes of use, geographically averaged on a study-area-wide basis, that the incumbent local exchange carrier experiences based on the prior year's annual use. Tandem-switched transport transmission charges that are not presumed reasonable shall be suspended and investigated absent a substantial cause showing by the incumbent local exchange carrier.

(ii) In study areas where the incumbent local exchange carrier has implemented density pricing zones as described in section 69.124, per-minute common transport charges described in paragraph (a)(2)(i) of this section shall be presumed reasonable if the incumbent local exchange carrier bases the charges on a weighted per-minute equivalent of direct-trunked transport DS1 and DS3 rates that reflects the relative number of DS1 and DS3 circuits used in the tandem to end office links (or a surrogate based on the proportion of copper and fiber facilities in the interoffice network), calculated using the total actual voice-grade minutes of use, averaged on a zone-wide basis, that the incumbent local exchange carrier experiences based on the prior year's annual use. Tandem-switched transport transmission charges that are not presumed reasonable shall be suspended and investigated absent a substantial cause showing by the incumbent local exchange carrier.

(d)(1) Through June 30, 1998, the tandem-switched transport transmission charges may be distance-sensitive. Distance shall be measured as airline distance between the serving wire center and the end office, unless the customer has ordered tandem-switched transport between the tandem office and the end office, in which case distance shall be measured as airline distance between the tandem office and the end office.

(2) Beginning July 1, 1998, the per-minute charge for transport of traffic over common transport facilities described in paragraph (a)(2)(i) of this section may be

distance-sensitive. Distance shall be measured as airline distance between the tandem switching office and the end office.

(e)(1) Through June 30, 1998, if the telephone company employs distance-sensitive rates:

(i) A distance-sensitive component shall be assessed for use of the transmission facilities, including intermediate transmission circuit equipment between the end points of the interoffice circuit; and

(ii) A non-distance-sensitive component shall be assessed for use of the circuit equipment at the ends of the interoffice transmission links.

(2) Beginning July 1, 1998, if the telephone company employs distance-sensitive rates for transport of traffic over common transport facilities, as described in paragraph (a)(2)(i) of this section:

(i) A distance-sensitive component shall be assessed for use of the common transport facilities, including intermediate transmission circuit equipment between the end office and tandem switching office; and

(ii) A non-distance-sensitive component shall be assessed for use of the circuit equipment at the ends of the interoffice transmission links.

(f) [Reserved.]

(g)(1) The tandem switching charge imposed pursuant to paragraphs (a)(1) or (a)(2)(ii) of this section, as applicable, shall be set to recover twenty percent of the annual part 69 interstate tandem revenue requirement plus one third of the portion of the tandem switching revenue requirement being recovered through the interconnection charge recovered by §§ 69.124, 69.153, and 69.155, excluding multiplexer and dedicated port costs recovered in accordance with paragraph (l) of this section.

(2) Beginning January 1, 1999, the tandem switching charge imposed pursuant to paragraph (a)(2)(ii) of this section shall be set to recover the amount prescribed in paragraph (g)(1) of this section plus one half of the remaining portion of the tandem switching revenue requirement then being recovered through the interconnection charge recovered by §§ 69.124, 69.153, and 69.155, excluding multiplexer and dedicated port costs recovered in accordance with paragraph (l) of this section.

(3) Beginning January 1, 2000, the tandem switching charge imposed pursuant to paragraph (a)(2)(ii) of this section shall be set to recover the entire interstate tandem

switching revenue requirement, including that portion formerly recovered through the interconnection charge recovered in §§ 69.124, 69.153, and 69.155, and excluding multiplexer and dedicated port costs recovered in accordance with paragraph (l) of this section.

(4) A local exchange carrier that is subject to price cap regulation as that term is defined in § 61.3(x) of this chapter shall calculate its tandem switching revenue requirement as used in this paragraph by dividing the tandem switching revenue requirement that was included in the original interconnection charge by the original interconnection charge, and then multiplying this result by the annual revenues recovered through the interconnection charge, described in § 69.124, as of June 30, 1997.

* * * * *

(l) In addition to the charges described above, price cap local exchange carriers shall establish separate charges for multiplexers and dedicated trunk ports used in conjunction with the tandem switch as follows:

(1) Local exchange carriers must establish a traffic-sensitive charge for DS3/DS1 multiplexers used on the end office side of the tandem switch, assessed on purchasers of common transport to the tandem switch. This charge must be expressed in dollars and cents per access minute of use. The maximum charge shall be calculated by dividing the total costs of the multiplexers on the end office-side of the tandem switch by the serving wire center side of the tandem switch by the projected annual access minutes of use calculated for purposes of recovery of common transport costs in paragraph (c) of this section. A similar charge shall be assessed for DS1/voice-grade multiplexing provided on the end-office side of analog tandem switches.

(2)(i) Local exchange carriers must establish a flat-rated charge for dedicated DS3/DS1 multiplexing on the serving wire center side of the tandem switch provided in conjunction with dedicated DS3 transport service from the serving wire center to the tandem switch. This charge shall be assessed on interexchange carriers purchasing tandem-switched transport in proportion to the number of DS3 trunks provisioned for that interexchange carrier between the serving wire center and the tandem-switch.

(ii) Local exchange carriers must establish a flat-rated charge for dedicated DS1/voice-grade multiplexing provided on the serving wire center side of analog tandem switches. This charge may be assessed on interexchange carriers purchasing tandem-switched transport in proportion to the interexchange carrier's transport capacity on the serving wire center side of the tandem.

(3) Price cap local exchange carriers may recover the costs of dedicated trunk ports on the serving wire center side of the tandem switch only through flat-rated charges expressed in dollars and cents per trunk port and assessed upon the purchaser of the dedicated trunk terminating at the port.

18. Section 69.122 is removed.

19. Section 69.123 is amended by adding paragraph (f) to read as follows:

§ 69.123 Density pricing zones for special access and switched transport.

* * * * *

(f)(1) An incumbent local exchange carrier that establishes density pricing zones under this section must reallocate additional amounts recovered under the interconnection charge prescribed in § 69.124 to facilities-based transport rates, reflecting the higher costs of serving lower-density areas. Each incumbent local exchange carrier must reallocate costs from the interconnection charge each time it increases the differential between prices in density zones two and one or between three and one.

(2) Any incumbent local exchange carrier that has already deaveraged its rates on the date these rules become effective must reallocate an amount equivalent to that described in paragraph (f)(1) of this section from the interconnection charge prescribed in § 69.124 to its transport services.

(3) Price cap local exchange carriers shall reassign to direct-trunked transport and tandem-switched transport categories or subcategories interconnection charge amounts reallocated under paragraph (f)(1) or (f)(2) of this section in a manner that reflects the way density pricing zones are being implemented by the incumbent local exchange carrier.

20. Section 69.124 is revised to read as follows:

§ 69.124 Interconnection charge.

(a) For telephone companies not subject to price cap regulation, an interconnection charge expressed in dollars and cents per access minute shall be assessed upon all interexchange carriers and upon all other persons using the telephone company local transport network.

(b) For telephone companies not subject to price cap regulation, the interconnection charge shall be computed by subtracting entrance facilities, tandem-switched transport, direct-trunked transport, and dedicated signalling transport revenues from the Part 69 transport revenue requirement, and dividing by the total interstate local transport minutes.

21. Section 69.125 is amended by revising paragraph (a) to read as follows:

§ 69.125 Dedicated signalling transport.

(a) Dedicated signalling transport shall consist of two elements, a signalling link charge and a signalling transfer point (STP) port termination charge.

* * * * *

22. Section 69.126 is revised to read as follows:

§ 69.126 Nonrecurring charges.

Incumbent local exchange carriers shall not assess any nonrecurring charges for service connection when an interexchange carrier converts trunks from tandem-switched transport to direct-trunked transport or when an interexchange carrier orders the disconnection of overprovisioned trunks, until six months after the effective date of the tariffs eliminating the unitary pricing option for tandem-switched transport.

22.a. Section 69.201, 69.203, 69.204, 69.205 and 69.209 are removed.

23. Subpart C is revised by adding sections 69.151, 69.152, 69.153, 69.154, 69.155, 69.156 and 69.157 to read as follows:

SUBPART C -- COMPUTATION OF CHARGES FOR PRICE CAP LOCAL EXCHANGE CARRIERS

SUBPART C -- COMPUTATION OF CHARGES FOR PRICE CAP LOCAL EXCHANGE CARRIERS

§ 69.151 Applicability.

This subpart shall apply only to telephone companies subject to the price cap regulations set forth in Part 61 of this chapter.

§ 69.152 End user common line for price cap local exchange carriers.

(a) A charge that is expressed in dollars and cents per line per month shall be assessed upon end users that subscribe to local exchange telephone service or Centrex service to the extent they do not pay carrier common line charges. A charge that is expressed in dollars and cents per line per month shall be assessed upon providers of public telephones. Such charge shall be assessed for each line between the premises of an end user, or public telephone location, and a Class 5 office that is or may be used for local exchange service transmissions.

(b) Except as provided in paragraphs (d) through (i) of this section, the maximum single line rate or charge shall be computed:

(1) By dividing one-twelfth of the projected annual revenue requirement for the End User Common Line element by the projected average number of local exchange service subscriber lines in use during such annual period, only so long as a per-minute carrier common line charge is assessed or the multi-line PICC defined in § 69.153 recovers common line revenues.

(2) By dividing one-twelfth of the projected annual revenues permitted for the common line basket under the Commission's price cap rules, as set forth in part 61 of this chapter, by the projected average number of local exchange service subscriber lines in use during such annual period, if no per-minute carrier common line charge is assessed and the multi-line PICC defined in § 69.153 does not recover any common line revenues.

(3) Provided, however, that the charge for each local exchange service subscriber line shall not exceed $9.00 as adjusted by the inflation factor computed under paragraph (k) of this section.

(c) The charge for each subscriber line associated with a public telephone shall be equal to the monthly charge computed in accordance with paragraph (b) of this section.

(d)(1) Through December 31, 1997, the monthly charge for each primary residential or single line business local exchange service subscriber line shall be the charge computed in accordance with paragraph (b) of this section, or $3.50, whichever is lower.

(2) Beginning January 1, 1998, the maximum monthly charge for each primary residential or single line business local exchange service subscriber line shall be the charge computed in accordance with paragraph (b) of this section, or $3.50, whichever is lower.

(e)(1) Through December 31, 1997, the monthly charge for each non-primary residential local exchange service subscriber line shall be the charge computed in accordance with paragraph (b) of this section, or $3.50, whichever is lower.

(2) Beginning January 1, 1998, the maximum monthly charge for each non-primary residential local exchange service subscriber line shall be the lower of:

(i) The maximum charge computed in accordance with paragraph (b) of this section; or

(ii) $5.00. On January 1, 1999, this amount shall be adjusted by the inflation factor computed under paragraph (k) of this section, and increased by $1.00. On July 1, 2000, and in each subsequent year, this amount shall be adjusted by the inflation factor computed under paragraph (k) of this section, and increased by $1.00.

(3) Where the local exchange carrier provides a residential line to another carrier so that the other carrier may resell that residential line to a residence that already receives a primary residential line, the local exchange carrier may collect the non-primary residential charge described in paragraph (e) of this section from the other carrier.

(f) Except as provided in paragraphs (n) and (o) of this section, the charge for each primary residential local exchange service subscriber line shall be the same as the charge for each single line business local exchange service subscriber line.

(g) A line shall be deemed to be a residential subscriber line if the subscriber pays a rate for such line that is described as a residential rate in the local exchange service tariff.

(h) [Reserved.]

(i) A line shall be deemed to be a single line business subscriber line if the subscriber pays a rate that is not described as a residential rate in the local exchange service tariff and does not obtain more than one such line from a particular telephone company.

(j) No charge shall be assessed for any WATS access line.

(k)(1) On January 1, 1999:

(i) The ceiling for multi-line business subscriber lines under paragraph (b)(3) of this section will be adjusted to reflect inflation as measured by the change in GDP-PI for the 18 months ending September 30, 1998.

(ii) The ceiling for non-primary residential subscriber lines under paragraph (e)(2)(ii) of this section will be adjusted to reflect inflation as measured by the change in GDP-PI for the 12 months ending September 30, 1998.

(2) On July 1, 2000, the ceiling for multi-line business subscriber lines and non-primary residential subscriber lines will be adjusted to reflect inflation as measured by the change in GDP-PI for the 18 months ending on March 31, 2000.

(3) On July 1 of each subsequent year, the ceiling for multi-line business subscriber lines and non-primary residential subscriber lines will be adjusted to reflect inflation as measured by the change in GDP-PI for the 12 months ending on March 31 of the year the adjustment is made.

(l)(1) Beginning January 1, 1998, local exchange carriers shall assess no more than one end user common line charge as calculated under the applicable method under paragraph (e) of this section for Basic Rate Interface integrated services digital network (ISDN) service.

(2) Local exchange carriers shall assess no more than five end user common line charges as calculated under paragraph (b) of this section for Primary Rate Interface ISDN service.

(m) In the event the local exchange carrier charges less than the maximum end user common line charge for any subscriber lines, the local exchange carrier may not recover the difference between the amount collected and the maximum from carrier common line charges or PICCs.

(n) Through December 31, 1997, the End User Common Line charge for a residential subscriber shall be 50% of the charge specified in § 69.152(b) and (d) if the residential local exchange service rate for such subscribers is reduced by an equivalent amount, provided that such local exchange service rate reduction is based upon a means test that is subject to verification.

(o) Paragraphs (o)(1) and (o)(2) of this section are effective through December 31, 1997.

(1) The End User Common Line charge for residential subscribers shall be reduced to the extent of the state assistance as calculated in paragraph (o)(2) of this section, or waived in full if the state assistance equals or exceeds the residential End User Common Line charge under the circumstances described below. In order to qualify for this waiver, the subscriber must be eligible for and receive assistance or benefits provided pursuant to a narrowly targeted telephone company lifeline assistance program, requiring verification of eligibility, implemented by the state or local telephone company. A state or local telephone company wishing to implement this End User Common Line reduction or waiver for its subscribers shall file information with the Commission Secretary demonstrating that its plan meets the criteria set out in this section and showing the amount of state assistance per subscriber as described in paragraph (o)(2) of this section. The reduction or waiver of the End User Common Line charge shall be available as soon as the Commission certifies that the state or local telephone plan satisfies the criteria set out in this subsection and the relevant tariff provisions become effective.

(2)(i) The state assistance per subscriber shall be equal to the difference between the charges to be paid by the participating subscribers and those to be paid by other subscribers for comparable monthly local exchange service, service connections and customer deposits, except that benefits or assistance for connection charges and deposit requirements may only be counted once annually. In order to be included in calculating the state assistance, such benefits must be a single telephone line to the household's principal residence.

(ii) The monthly state assistance per participating subscriber shall be calculated by adding the amounts calculated in paragraphs (o)(2)(ii)(A) and (o)(2)(ii)(B) of this section.

(A) The amount of the monthly state assistance per participating subscriber for local exchange service shall be calculated by dividing the annual difference between charges paid by all participating subscribers for residential local exchange service and the amount which would have been charged to non-qualifying subscribers for comparable service by twelve times the number of subscribers participating in the state assistance program. Estimates may be used when historic data are not available.

(B) The amount of the monthly state assistance for service connections and customer deposits per participating subscriber shall be calculated by determining the annual amount of the reductions in these charges for participating subscribers each year and dividing this amount by twelve times the number of participating subscribers. Estimates may be used when historic data are not available.

(p) Through December 31, 1997, in connection with the filing of access tariffs pursuant to § 69.3(a), telephone companies shall calculate for the association their projected revenue requirement attributable to the operation of § 69.104(n) through (o). The projected amount will be adjusted by the association to reflect the actual lifeline assistance benefits paid in the previous period. If the actual benefits exceeded the projected amount for that period, the differential will be added to the projection for the ensuing period. If the actual benefits were less than the projected amount for that period, the differential will be subtracted from the projection for the ensuing period. Through December 31, 1997, the association shall so adjust amounts to the Lifeline Assistance revenue requirement, bill and collect such amounts from interexchange carriers pursuant to § 69.117 and distribute the funds to qualifying telephone companies pursuant to § 69.603(d).

§ 69.153 Presubscribed interexchange carrier charge (PICC).

(a) A charge expressed in dollars and cents per line may be assessed upon the subscriber's presubscribed interexchange carrier to recover the common line revenues permitted under the price cap rules in part 61 of this chapter that cannot be recovered through the end user common line charge established under § 69.152, residual interconnection charge revenues, and certain marketing expenses described in § 69.156(a). In the event the ceilings on the PICC prevent the PICC from recovering all the residual common line, residual interconnection charge revenues, and marketing expenses, the PICC shall recover all residual common line revenues before it recovers residual interconnection charge revenues, and all residual interconnection charge revenues before it recovers marketing expenses.

(b) If an end-user customer does not have a presubscribed interexchange carrier, the local exchange carrier may collect the PICC directly from the end user.

(c) The maximum monthly PICC for primary residential subscriber lines and single-line business subscriber lines shall be the lower of:

(1) One twelfth of the sum of annual common line revenues and residual interconnection charge revenues permitted under our price cap rules divided by the projected average number of local exchange service subscriber lines in use during such annual period, minus $3.50; or

(2) $0.53. On January 1, 1999, this amount shall be adjusted by the inflation factor computed under paragraph (e) of this section, and increased by $0.50. On July 1, 2000, and in each subsequent year, this amount shall be adjusted by the inflation factor computed under paragraph (e) of this section, and increased by $0.50.

(d) To the extent that a local exchange carrier cannot recover its full common line revenues, residual interconnection charge revenues, and those marketing expense revenues described in § 69.156(a) permitted under price cap regulation through the recovery mechanisms established in §§ 69.152, 69.153(c), and 69.156(b) and (c), the local exchange carrier may assess a PICC on multi-line business subscriber lines and non-primary residential subscriber lines.

(1) The maximum monthly PICC for non-primary residential subscriber lines shall be the lower of:

(i) One twelfth of the annual common line, residual interconnection charge, and § 69.156(a) marketing expense revenues permitted under our price cap rules, less the maximum amounts permitted to be recovered through the recovery mechanisms under §§ 69.152, 69.153(c), and 69.156(b) and (c), divided by the total number of projected non-primary residential and multi-line business subscriber lines in use during such annual period; or

(ii) $1.50. On January 1, 1999, this amount shall be adjusted by the inflation factor computed under paragraph (e) of this section, and increased by $1.00. On July 1, 2000, and in each subsequent year, this amount shall be adjusted by the inflation factor computed under paragraph (e) of this section, and increased by $1.00.

(2) If the maximum monthly PICC for non-primary residential subscriber lines is determined using paragraph (d)(1)(i) of this section, the maximum monthly PICC for multi-line business subscriber lines shall equal the maximum monthly PICC of non-primary residential subscriber lines. Otherwise, the maximum monthly PICC for multi-line business lines shall be the lower of:

(i) One twelfth of the annual common line, residual interconnection charge, and § 69.156(a) marketing expense revenues permitted under parts 61 and 69 of our rules, less the maximum amounts permitted to be recovered through the recovery mechanisms under §§ 69.152, 69.153(c) and (d)(1)(i), and 69.156 (b) and (c), divided by the total number of projected multi-line business subscriber lines in use during such annual period; or

(ii) $2.75. On January 1, 1999, this amount shall be adjusted by the inflation factor computed under paragraph (e) of this section, and increased by \$1.50. On July 1, 2000, and in each subsequent year, this amount shall be adjusted by the inflation factor computed under paragraph (e) of this section, and increased by \$1.50.

(e) For the PICC ceiling for primary residential subscriber lines and single-line business subscriber lines under paragraph (c)(2) of this section, non-primary residential subscriber lines under paragraph (d)(1)(ii) of this section, and multi-line business subscriber lines under paragraph (d)(2)(ii) of this section:

(1) On January 1, 1999, the ceiling will be adjusted to reflect inflation as measured by the change in GDP-PI for the 12 months ending September 30, 1998.

(2) On July 1, 2000, the ceiling will be adjusted to reflect inflation as measured by the change in GDP-PI for the 18 months ending on March 31, 2000.

(3) On July 1 of each subsequent year, the ceiling will be adjusted to reflect inflation as measured by the change in GDP-PI for the 12 months ending on March 31 of the year the adjustment is made.

(f)(1) Local exchange carriers shall assess no more than one PICC as calculated under the applicable method under paragraph (d)(1) of this section for Basic Rate Interface integrated services digital network (ISDN) service.

(2) Local exchange carriers shall assess no more than five PICCs as calculated under paragraph (d)(2) of this section for Primary Rate Interface ISDN service.

§ 69.154 Per-minute carrier common line charge.

(a) Local exchange carriers may recover a per-minute carrier common line charge from interexchange carriers, collected on originating access minutes and calculated using the weighting method set forth in paragraph (c) of this section. The maximum such charge shall be the lower of:

(1) The per-minute rate that would recover annual common line revenues permitted less the maximum amounts allowed to be recovered under §§ 69.152 and 69.153; or

(2) The sum of the local switching, carrier common line and interconnection charge charges assessed on originating minutes on December 31, 1997, minus the local switching charges assessed on originating minutes.

(b) To the extent that paragraph (a) of this section does not recover from interexchange carriers all permitted carrier common line revenue, the excess may be collected through a per-minute charge on terminating access calculated using the weighting method set forth in paragraph (c) of this section.

(c) For each Carrier Common Line access element tariff, the premium originating Carrier Common Line charge shall be set at a level that recovers revenues allowed under paragraphs (a) and (b) of this section. The non-premium charges shall be equal to .45 multiplied by the premium charges.

§ 69.155 Per-minute residual interconnection charge.

(a) Local exchange carriers may recover a per-minute residual interconnection charge on originating access. The maximum such charge shall be the lower of:

(1) The per-minute rate that would recover the total annual residual interconnection charge revenues permitted less the portion of the residual interconnection charge allowed to be recovered under § 69.153; or

(2) The sum of the local switching, carrier common line and residual interconnection charges assessed on originating minutes on December 31, 1997, minus the local switching charges assessed on originating minutes, less the maximum amount allowed to be recovered under § 69.154(a).

(b) To the extent that paragraph (a) of this section prohibits a local exchange carrier from recovering all of the residual interconnection charge revenues permitted, the residual may be collected through a per-minute charge on terminating access.

(c) Any charge assessed pursuant to paragraphs (a) or (b) of this section shall be assessed only upon minutes utilizing the local exchange carrier's local transport service.

§ 69.156 Marketing expenses.

(a) Local exchange carriers shall recover marketing expenses that are allocated to the common line and traffic sensitive baskets, and the switched services within the trunking basket pursuant to §§ 32.6610 of this chapter and 69.403.

(b) The expenses described in paragraph (a) of this section may be recovered from non-primary residential subscriber lines, by increasing the end user common line charge described in § 69.152(e). The amount of marketing expenses permitted to be recovered in this manner shall be the total marketing expenses described in paragraph (a) of this section divided by the sum of non-primary residential lines and multi-line business lines. In no event shall the end user common line charge for these lines exceed the lower of the ceilings established in § 69.152(b)(3) and (e)(2)(ii).

(c) The expenses described in paragraph (a) of this section may be recovered from multi-line business subscriber lines, by increasing the end user common line charge described in § 69.152(b). The amount permitted to be recovered in this manner shall be the total marketing expenses described in paragraph (a) of this section divided by the sum of non-primary residential lines and multi-line business lines. In no event shall the end user common line charge for these lines exceed the ceiling established in § 69.152(b)(3).

(d) In the event that the ceilings set forth in paragraphs (b) and (c) of this section, and § 69.153(d) prevent a local exchange carrier from recovering fully the marketing expenses described in paragraph (a) of this section, the local exchange carrier may recover the remainder through a per-minute assessment on originating access minutes, so long as the charge for originating access does not exceed the amount defined in § 69.155(a)(2) less the maximum permitted to be recovered under § 69.155(a).

(e) In the event that the ceilings set forth in paragraphs (b), (c) and (d) of this section, and § 69.153(d) prevent a local exchange carrier from recovering fully the marketing expenses described in paragraph (a) of this section, the local exchange carrier may recover the remainder through a per-minute assessment on terminating access minutes.

(f) The amount of marketing expenses that may be recovered each year shall be adjusted in accordance with the price cap rules set forth in part 61 of this chapter.

§ 69.157 Line port costs in excess of basic, analog service.

To the extent that the costs of ISDN line ports, and line ports associated with other services, exceed the costs of a line port used for basic, analog service, local exchange carriers may recover the difference through a separate monthly end user charge.

24. Section 69.303 is amended by removing paragraph (a) and the designator "(b)".

25. Section 69.304 is amended by removing paragraph (c).

26. Section 69.305 is amended by revising paragraphs (b) and (d), and adding paragraph (e) to read as follows:

§ 69.305 Carrier cable and wire facilities (C&WF).

* * * * *

(b) Carrier C&WF, other than WATS access lines, not assigned pursuant to paragraphs (a), (c), or (e) of this section that is used for interexchange services that use switching facilities for origination and termination that are also used for local exchange telephone service shall be apportioned to the local Transport elements.

* * * * *

(d) All Carrier C&WF that is not apportioned pursuant to paragraphs (a), (b), (c), and (e) of this section shall be assigned to the Special Access element.

(e) Carrier C&WF that is used to provide transmission between the local exchange carrier's signalling transfer point and the local switch shall be assigned to the local switching category.

27. Section 69.306 is amended by revising paragraphs (c), (d), and (e) to read as follows:

§ 69.306 Central office equipment (COE).

* * * * *

(c) COE Category 2 (Tandem Switching Equipment) that is deemed to be exchange equipment for purposes of the Modification of Final Judgment in United States v Western Electric Co. shall be assigned to the tandem switching charge subelement and the interconnection charge element. COE Category 2 which is associated with the signal transfer point function shall be assigned to the local switching category. COE Category 2 which is used to provide transmission facilities between the local exchange carrier's signalling transfer point and the database shall be assigned to the Line Information Database subelement at § 69.120(a). All other COE Category 2 shall be assigned to the interexchange category.

(d) COE Category 3 (Local Switching Equipment) shall be assigned to the Local Switching element except as provided in paragraph (a) of this section; and that, for telephone companies subject to price cap regulation set forth in part 61 of this chapter, line-side port costs shall be assigned to the Common Line rate element.

(e) COE Category 4 (Circuit Equipment) shall be apportioned among the interexchange category and the Common Line, Transport, and Special Access elements. COE Category 4 shall be apportioned in the same proportions as the associated Cable and Wireless Facilities; except that any DS1/voice-grade multiplexer investment associated with analog local switches and assigned to the local transport category by this rule shall be reallocated to the local switching category.

28. Section 69.307 is amended by removing paragraph (c).

29. Section 69.308 is removed.

30. Section 69.309 is revised to read as follows:

§ 69.309 Other investment.

Investment that is not apportioned pursuant to §§ 69.302 through 69.307 shall be apportioned among the interexchange category, the billing and collection category and access elements in the same proportions as the combined investment that is apportioned pursuant to §§ 69.303 through 69.307.

31. Section 69.401 is amended by revising paragraph (b) to read as follows:

§ 69.401 Direct expenses.

* * * * *

(b) Plant Specific Operations Expenses in Accounts 6210, 6220 and 6230, shall be apportioned among the interexchange category and access elements on the basis of the apportionment of the investment in Accounts 2210, 2220, and 2230, respectively; provided that any expenses associated with DS1/voice-grade multiplexers, to the extent that they are not associated with an analog tandem switch, assigned to the local transport category by this subsection shall be reallocated to the local switching category; provided further that any expenses associated with common channel signalling included in Account 6210 shall be assigned to the local transport category.

* * * * *

32. Section 69.406 is amended by removing paragraph (a)(9).

33. Section 69.410 is removed.

34. Section 69.411 is revised to read as follows:

§ 69.411 Other expenses.

Except as provided in §§ 69.412, 69.413, and 69.414, expenses that are not apportioned pursuant to §§ 69.401 through 69.409 shall be apportioned among the interexchange category and all access elements in the same manner as § 69.309 Other investment.

35. Section 69.501 is amended by removing and reserving paragraph (a).

36. Section 69.502 is revised to read as follows:

§ 69.502 Base factor allocation.

Projected revenues from the following shall be deducted from the base factor portion to determine the amount that is assigned to the Carrier Common Line element:

(a) End User Common Line charges, less any marketing expense revenues recovered through end user common line charges pursuant to § 69.156;

(b) Special Access surcharges; and

(c) The portion of frozen per-line support that carriers receive pursuant to § 54.303 that is attributable to LTS payments received prior to January 1, 1998.

37. Section 69.611 is removed.

May 7, 1997

Statement of
Commissioner James H. Quello

RE: FEDERAL-STATE JOINT BOARD ON UNIVERSAL SERVICE (CC Docket No. 96-45),

ACCESS CHARGE REFORM (CC Docket No. 96-262), and

PRICE CAP PERFORMANCE REVIEW FOR LOCAL EXCHANGE CARRIERS (CC Docket No. 94-1).

Today, the Commission has established rules to implement the Universal Service provisions of the Telecommunications Act of 1996, as well as rules to restructure the access charge system while also initiating reductions in the levels of those access charges. I have believed throughout my participation in the debates regarding universal service and access reform that, as much as possible, we should seek to ensure that consumers experience the benefits of our actions. To this same end, we should try to avoid the possibility that total bills for groups of consumers could increase as a result of implementing new universal service programs and moving into a new access charge regime.

Universal Service

This Commission now has taken steps to establish processes for the administration of universal service funds in a way that allows the commitments represented in this section of the 1996 Telecommunications Act to be fulfilled. We have labored to develop a reasonable plan that will provide necessary and sufficient funds for schools and libraries as well as other universal service programs. We also have sought to avoid collection of funds beyond those legitimately needed to help make new and important services available to students and teachers in inner city, suburban and rural schools from Takoma Park, D.C., to Tacoma, Washington, from McAllen, Texas to Mackinac Island on the Upper Peninsula of Michigan.

We have achieved this balance by establishing funding necessary to begin the program at a reasonable level, with a provision that allows schools and libraries to begin the program January 1, 1998. By this time, we would hope that participating groups will have had the opportunity to develop their plans. Our decision to start the program with lower funding in the first six months, increasing in the following years, gives the program early constraint, with flexibility at later periods when greater demand is likely to develop. As a result, I believe this decision provides for new universal service funding within the limits of what consumers around the country are willing to pay.

The issue of what consumers are prepared to pay has been a very difficult one. The need for our attention to the issue, however, has been clearly expressed in many ways. It has required the Commission to balance the need for programs involved in universal service that are critically important to the future of this country with their cost. In this respect, this universal service proceeding is one of the most important decisions in this agency's history. At the same time, we have heard a consistent message from around the country that consumers and businesses are not necessarily willing to pay for these services through higher total bills for telecommunications services.

With respect to funding for health care subsidies, we have endeavored to make sure that rural, non-profit health care facilities have sufficient funding to meet the needs for providing services in communities that otherwise might not have the same resources that are available in urban communities.

There also are many other policy and market issues that will need to be resolved in a new universal service environment. For instance, I believe it remains to be seen how cable and wireless industries will continue to develop to play a greater role in the telecommunications services that will meet future universal service needs. As these developments occur, the Commission may continue to monitor the equity of contribution and recovery of universal service funds by paging services as well as the extent to which wireless services in general should contribute for intrastate services.

Access Reform

The Commission's actions today on access reform involve two components: (1) several structural changes that will cause access components to move to more reasonable categories and to become subject to competition where possible; and (2) reductions in the current level of access charges, largely accomplished through revision of the productivity and sharing mechanism in LEC price caps.

Where this decision changes the structure of end user charges, as in our treatment of business and residential customers, and consumers with second or multiple lines, I believe our decisions should be -- and are -- characterized by balance. As a result of this necessary reform of the access payment structure, charges should remain within reasonable bounds and should help to promote the development of competition and consumer benefits.

I also believe this Commission would be remiss in our regulatory duties to the American public and responsibilities to our licensees if we were to restructure universal service without concurrently engaging in access charge reform. We have talked about this step for quite some time. Many parties have expressed their views in a very public fashion as to whether or not this step is warranted, or to what degree access charges should be reduced. I believe that this step to restructure and reduce the level of access charges is the right thing to do and this is the right time to do it.

The consumers and users of telecommunications services are the intended beneficiaries of today's actions regarding access reform. Now that these decisions are adopted, I believe it will become clear that we have done our best to ensure that consumers do not bear the burden of implementing the new universal service program and access charge reform. Our actions also represent a fundamental part of the Commission's effort to facilitate competition in the local exchange marketplace, in this case by reducing access charges paid to LECs by interexchange carriers.

The primary vehicle for this reduction is the decision to change the existing combinations of productivity factors, or "x-factors", and sharing options to a single productivity factor of 6.5% accompanied by no sharing obligation. As a result, this decision continues the Commission's efforts to move away from the lingering remnants of rate of return regulation for local exchange carriers. Today's decision will complete the movement of price cap LECs away from the sharing obligations that were part of the past system.

Looking to the Future

I want to emphasize that today's actions represent a first step in many respects.

Concerning universal service, this is not a day to declare victory. There is much left to be done by the Commission, the states, temporary and permanent fund administrators, school districts, libraries, health care facilities, parties developing cost models, and telecommunications companies seeking to provide services and enter new markets. This is definitely an important day, but the real effort is just beginning. That effort will require investment, planning, training in using services, and community, professional, and corporate involvement, and it will only be successful after the continuing involvement, in community after community, by the many parties who have so diligently participated in this proceeding.

The Commission's action to increase the productivity factor not only results in reduced access charges in the first year, but also in further reductions in access charges in subsequent years. In another respect, it may very well become necessary very soon for the Commission to consider how to supplement today's decision to allow for pricing flexibility by LECs as competition develops to a greater level in the local marketplace. One possible way to provide that flexibility might be through relaxing the 6.5% productivity factor where LECs can meet criteria to demonstrate sufficient competition.

At the same time, later steps might also include the potential for checks and balances in the event that competition in the local exchange marketplace does not develop as soon as some seem to expect. Once again, down the road the Commission may need to consider more specific measures to ensure that the platforms necessary for competition truly are available. It is my hope that those steps won't be necessary.

Finally, some parties have warned recently that any actions by this Commission to lower access charges may cause LECs to seek to raise local phone rates. That matter will become an issue for state commissions, and it is my hope that they will respond to any efforts to raise local rates by ensuring that consumers ultimately benefit from federal and state actions to implement the Telecommunications Act of 1996 and any related decisions.

May 7, 1997

Separate Statement
of
Commissioner Susan Ness

Re: Universal Service; Access Reform; Price Cap Review

Today we reach another milestone in our efforts to secure for consumers the myriad benefits made possible by the Telecommunications Act of 1996. We are steadfastly fulfilling the tasks assigned to us by Congress in a manner that will prove the wisdom -- and realize the vision -- of this landmark legislation.

Our pursuit has many facets. We must eliminate impediments to competition, ensure fair rules of engagement for all market participants, safeguard the interests of residential consumers, especially those with limited incomes and those in high cost areas, promote economic efficiency, and lower prices to consumers. Today's orders represent substantial progress on all these fronts.

Much of what we are doing is driven by law and by economics. But the results of our decisions have a human face:

> Will a poor family in Appalachia be able to summon the police or fire department in an emergency?
>
> Will a critically ill patient in a remote region of Montana have her tumor quickly and accurately diagnosed?
>
> Will a curious high-school freshman have an opportunity to view Thomas Jefferson's valedictory letter, in his own aged but still powerful hand?
>
> Will an elderly widow be less hesitant to break her loneliness with longer and more frequent calls to her great-grandchildren?

Today brings us closer to a day when these questions can all be answered "yes."

Fifteen months after enactment of the Telecommunications Act, the transition to a new industry paradigm remains far from complete. The road is not straight, or smooth, or free from peril. But a steady course -- and a shared determination -- can bring us to the desired destination.

We still have far to travel to resolve issues of support for high-cost areas. I believe we have a sound plan and a clear timetable for implementation, but we still face two main obstacles. The proxy models, already impressive feats of cost engineering, still require further refinement before they can reliably be used to target federal cost support. And a new consensus must be achieved before support essential to maintain affordable telephone service in high-cost states can be drawn from states with lesser need, as I believe the Congress of the United States clearly intended. In the meantime, we can make only incremental changes in the implicit subsidies that currently support the high-cost services provided by large price cap telephone companies.

For the smaller rural companies, change will come even more gradually. This is consistent with Congress's expectation that competition would arrive more quickly in the cities and the suburbs. In the interim, we recognize that rural economies must not face unnecessary dislocations.

The need to avoid harmful dislocations, while also encouraging beneficial change, is crucial to much of what we are doing in the access reform and price cap orders. We are implementing many changes that will help to ensure an orderly transition from monopoly to fair and efficient competition.

In particular, the recovery of more costs through flat-rated charges instead of usage-sensitive charges will reduce the exposure of incumbent telephone companies to "cherry-picking" by new entrants, even as they also expand the range of customers likely to be offered competitive alternatives. Completion of the conversion to a three-part rate structure for tandem-switched transport will eliminate a historical artifact, but allow time for affected carriers to adjust. The new X-factor more accurately reflects the productivity gains that can reasonably be expected from price cap carriers, while avoiding radical reduction of telephone company access revenues and proposals that would have unfairly penalized those companies that have most assiduously conducted themselves in accordance with the incentives we deliberately created.

We prefer to rely on marketplace forces rather than regulation to drive investment decisions and price reductions. Some will fault us for not acting more aggressively; others will complain that we are too heavy-handed. My own view is that each decision, and all of the many issues in these orders, has been approached with balance and sensitivity, fairness and principle.

Not everyone will be satisfied. But no one can say that we have not read the law, considered economic theories and business realities, consulted our consciences, and sought to achieve as much fairness as is humanly possible.

I readily confess that I cannot muster the same passion for restructuring the arcane and impenetrable Transport Interconnection Charge as for devising a completely new regime to provide discounts for schools and libraries to access telecommunications and information services. Though I am fully committed to full realization of all of the universal service provisions, the Snowe-Rockefeller-Exon-Kerry provisions reflect an especially bold vision.

For our part, we have used our creativity to harness the magic of competition to reduce the costs of the support program, created incentives to ensure only prudent use of supported services, targeted discounts to minimize the danger of a widening gap between information haves and have-nots, and sought at every turn to maintain our commitment to competitive neutrality.

Even more important, we have sought to leave crucial decisions in the hands of educators and librarians, scattered throughout the country, rather than in the hands of Washington-based administrators. And, best of all, we have arranged a smooth take-off that will avoid creating unsustainable financial burdens on carriers and consumers, allowing competition and growth and declining prices -- rather than rate increases -- to supply the necessary funds.

In this area, as in the others addressed by today's orders, we have applied all our energy, and all our skill, to make the best decisions, based on our current knowledge and the law. A continuing commitment to constructive dialogue by all interested parties -- telephone companies, long distance companies, wireless companies, small businesses, large businesses, residential consumers, state regulators, and members of Congress -- is critical to continued progress. At the end of the day, fairness to all parties and demonstrable benefits to consumers are the standards by which we will all be judged.

May 7, 1997

Separate Statement of

Commissioner Rachelle B. Chong

Re: *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges, First Report and Order,* CC Docket Nos. 96-262, 94-1, 91-213, 95-72.

The Commission's access charge system has been a constant landmark in the telecommunications regulatory landscape during the past decade. Charges imposed by this access charge regime were unduly high, because these access charges were part of the funding mechanism for our patchwork quilt "system" of universal service funding.

With the passage of the Telecommunications Act of 1996 ("1996 Act"), however, the days of the current access charge system became numbered. The 1996 Act directed the Commission to create a universal service program that makes sense in a competitive marketplace.[800] Thus, it is appropriate and necessary for the Commission to do a thorough overhaul of our access charge regime in concert with implementation of the new universal service system ordered by the 1996 Act. To the extent possible, implicit subsidies must be identified and removed from access charges, and a sensible transition made to a market forces system where access charges are based on forward-looking economic cost. While I believe that today's decision generally finds the right balance in creating an improved access charge system, I write separately to explain our actions and comment on some aspects of our decision.

In this order, we direct that federal universal service support received by incumbent local exchange telephone carriers be used to reduce the interstate revenue requirement otherwise collected through interstate access charges. Thus, interstate implicit support will be identified and removed from interstate access charges, and instead we will provide universal service support through an explicit support mechanism ordered in our companion *Universal Service* decision.

The existence of universal service support subsidies within access charges, however, only partially explains why access charges create distortions in the marketplace and vast economic inefficiencies. Other culprits which drive access charges up for interexchange carriers include the current rate structures and pricing levels of our access charge system. These overly high charges are eventually passed through to long distance consumers in the

[800] 47 U.S.C. Section 254 (e)(requiring that any universal service support "be explicit and sufficient to achieve the purposes of this section").

form of a higher per minute usage rate. This overly high usage rate unduly suppresses demand for long distance services.

Our actions today – both in this docket and the price cap proceeding – should bring about a significant drop in access charges and create favorable conditions for competitive entry into the access market. I strongly supported efforts to push the inflated access rates downwards closer towards forward-looking economic cost. While some parties demanded immediate deep cuts in access charges, we have chosen a more measured approach for the transitional period.

First, we create a framework to remove distortions and inefficiencies in the current rate structures and levels, by attempting to ensure that the rates for access are more reflective of the way that costs are actually incurred. Second, we will move residual costs that were traditionally recovered on a per-minute basis into a more efficient flat-rate charge system that will result in lower per minute usage rates. During the early years of our transition, we have targeted business and multiline residential customers to bear the greater share of the burden, in order to keep rates affordable to single line residential and single line business customers.

My one major concern about today's approach is the impact that these increased flat rate charges will have on small business consumers during the early years of the transition. Because the Commission has decided to protect single line customers from any rate increases, the new flat rate charges fall disproportionately upon the shoulders of multiline customers and may have a disparate impact on small businesses who may not be able to afford these costs. I have advocated lessening the impact of the new subscriber line charge levels and flat charges on small businesses, particularly those who do not make many long distance calls and will not experience the full benefits of lower per minute calling rates that will be realized by large businesses with high call volumes. While I believe we cushioned the impact on small businesses to some extent, I acknowledge that some small businesses with low volume calling patterns may see some rate increases. While unfortunate, this is the price we pay for protection of the single line customers.

In sum, we have adopted what I believe to be a balanced and fair approach to access charge restructuring, universal service, and price cap adjustments. We have attempted to accomplish a massive overhaul to both the access charge and universal service systems with the least amount of disruption to consumers. Nevertheless, it is unfortunate but inevitable that there will be some discombobulation as we make a transition to a more competitive marketplace. Ultimately, however, I am confident that the journey to the new competitive world mandated by the 1996 Act will be worthwhile for consumers, as costs flow where they should, and rates readjust to where the market drives them.